UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

Form 10-K

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

For the fiscal year ended December 31, 2019
or

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

Commission file number 000-09587

ELECTRO-SENSORS, INC.

(Exact name of registrant as specified in its charter)

Minnesota	**41-0943459**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

6111 Blue Circle Drive
Minnetonka, Minnesota 55343-9108
(Address of principal executive offices, including zip code)

(952) 930-0100
(Registrant's telephone number)

Securities registered under Section 12(b) of the Exchange Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	ELSE	**Nasdaq Capital Market**

Securities registered under Section 12(g) of the Exchange Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. Yes ☐ No ☒

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 ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer ☐
Non-accelerated filer	☐	Smaller reporting company ☒
		Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The aggregate market value of the voting stock held by non-affiliates (persons other than officers, directors, or holders of more than 5% of the outstanding stock) of the registrant was approximately $7,400,000 based upon the closing price of its common stock as reported on The Nasdaq Stock Market® on June 30, 2019.

The number of shares outstanding of the registrant’s Common Stock, $0.10 par value, on March 24, 2020 was 3,395,521.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information called for by Part III of this Form 10-K is incorporated by reference from the registrant’s Definitive Proxy Statement, which will be filed pursuant to Regulation 14A not later than 120 days after the end of the fiscal year covered by this report.

ELECTRO-SENSORS, INC.
Form 10-K for the Year Ended December 31, 2019
TABLE OF CONTENTS

PART I

Item 1. Business.

Introduction

Electro-Sensors, Inc. (“we,” “us,” “our,” the “Company” or “ESI”) manufactures and sells industrial production monitoring and process control systems.

In addition, we may periodically make strategic investments in other businesses and companies, including investments that we believe would facilitate the development of technology complementary to our existing products or investments that we believe present good opportunities for the Company and its shareholders. Our primary focus is to remain an operating company and we do not intend to become an investment company.

ESI was incorporated in Minnesota in July 1968. Our executive offices are located at 6111 Blue Circle Drive, Minnetonka, Minnesota, 55343-9108. Our telephone number is (952) 930-0100.

Products

We manufacture and sell a variety of monitoring systems that measure machine production and operation rates, as well as systems that regulate the speed of related machines in production processes.

Our goal is to develop meaningful annual updates to our standard products.

We have a sales agreement with Motrona GmbH, a German control and interface devices manufacturer, under which we have the right to distribute Motrona products in the United States. These products interface with our products on various applications for motion monitoring.

Speed Monitoring Systems

Our speed monitoring systems compare revolutions per minute or speed against acceptable rates as determined by our customers. These systems vary in complexity, from simple systems that detect slow-downs or stoppages, to more sophisticated systems that warn of deviations from precise tolerances and that permit various subsidiary operations to be determined through monitoring shaft speed.

Our speed monitoring systems also include a line of products that measure production counts or rates, such as number of parts, gallons per minute, or board feet. These speed monitoring systems also include alarm systems, tachometers, and other devices that translate impulses from the sensors into alarm signals, computer inputs, or digital displays that are usable by the customer.

We have several products used in drive control systems that regulate the speed of motors on related machines in a production sequence to ensure that the performances of various operations are coordinated. The products consist of a line of digital control products for motors that require a complete closed loop PID (Proportional Integral Derivative) control. The closed loop controllers coordinate production speed among process motors and reduce waste.

Temperature Application Products

Our main temperature applications include bearing, gear box, and motor temperature monitoring sensors. These sensors alert an operator when the temperature exceeds or is less than a specified temperature.

Position Application Products

We also offer production monitoring devices that include a belt alignment and slide gate position monitor. The belt alignment monitor is used to determine if a belt is tracking correctly. The slide gate position monitor is used in plant operations to provide feedback of the position of a slide gate. One version has analog output and the second version has relay outputs that provide feedback of the position of a valve or control arm.

Vibration Monitoring Products

A vibration monitor alerts an operator when the vibration of a machine in a production system exceeds or is less than a specified level.

Tilt Switches

A tilt switch is designed to alert the operator when a storage bin or production system reaches a certain capacity.

Hazard Monitoring Systems

Electro-Sentry We offer the Electro-Sentry 1 and Electro-Sentry 16 hazard monitoring systems, which integrate our sensors for monitoring temperature, belt alignment, and shaft speed with programmable control logic and LED display interface to create a complete hazard monitoring system. These systems enable our customers to locate which part of their material handling system is operating incorrectly, typically in less than ten seconds, by using visual indication on the LED displays.

HazardPRO™ We market our wireless hazard technology monitoring system under the HazardPRO product name. This integrated hazard monitoring system captures and displays key information in an intuitive format allowing the user to quickly and comprehensively understand the status and history of its processes. The simple but powerful interface gives the user insight into its operations as it strives to maximize safety and facility runtime, while minimizing costs associated with unscheduled maintenance and unplanned downtime. Furthermore, the HazardPRO system has been approved for use in hazardous dust environments by a third-party nationally recognized testing laboratory.

The HazardPRO site system manager software efficiently collects data from sensors placed across a widely dispersed area of greater than 50 acres. We have also added a complete antenna pair mounting system to the product line for easy and accurate customer installation.

We expect to continue to expend resources to develop new products and to market new and existing products for use in a wide variety of monitoring applications.

Our corporate website, www.electro-sensors.com, provides significant product application information for our existing and prospective customers and our sales partners. Information on our website is not incorporated by reference herein and is not a part of this Form 10-K.

Marketing and Distribution

We sell our products primarily through both our internal sales team and a number of manufacturer's representatives and distributors located throughout the United States, Canada, Mexico, Bolivia, Chile, Colombia, Guatemala, Peru, United Kingdom, Ukraine, Egypt, Saudi Arabia, India, Indonesia, Australia, New Zealand, China, Taiwan, Korea, Vietnam, Malaysia, Philippines, and Singapore. Sales to customers outside the United States represented approximately 12% of our 2019 sales. We sell our products under the Electro-Sensors, Inc. brand as a range of products from simple sensors to complex integrated monitoring systems. Our customers are businesses in a wide variety of industries, including grain/feed/milling, bulk materials, manufacturing, food products, ethanol, power generation, and other processing industries.

We continue to explore new industries and applications within the current industries we serve to expand sales and may also consider acquiring compatible businesses or product lines as part of our growth strategy. In addition, we may make investments that we believe present good opportunities for the Company and its shareholders.

We believe that a wide variety of organizations could achieve significant savings in both time and materials by adding production monitoring and drive control technology to existing processes to coordinate the operation of related machines. We sell our products into both the "retro-fit" market and into new manufacturing or processing systems.

We advertise in national industrial periodicals that cover a range of industrial products and attend several local, national and international industry tradeshows throughout the year. We also use our corporate website and other related industry websites for advertising and marketing purposes.

Competition

We face substantial competition in the sale of our production monitoring systems from a broad range of industrial and commercial businesses. Many of these competitors are well established and have greater sales volume. Among our larger competitors are Danaher Controls, Red Lion Controls, 4B Elevator Components Ltd., and Durant Corporation. We believe our competitive advantages include our products' superior design and quality, and the fact that we sell our products as ready-to-install units that can be used in a wide range of applications. Our major disadvantages include the fact that our major competitors are larger, have better established names, have a broader range of sensing instruments, and have larger sales forces.

Suppliers

We purchase parts and materials for our systems from various manufacturers and distributors. In some instances, these materials are manufactured in accordance with our proprietary designs. Multiple sources of these parts and materials are generally available, and we, typically, do not depend on any single source for these supplies and materials. We have not experienced any significant problem of short supply or delays from our suppliers. However, due to the outbreak of the COVID-19 virus, we are concerned and closely watching lead times and availability of components, especially those components that our suppliers purchase from outside the United States. We are currently assessing our current inventory levels and taking actions to minimize disruptions to our supply chain, although such actions may not be successful.

Customers

We do not depend upon a single or a few customers for a material (10% or more) portion of our sales. The extent of the impact of COVID-19 on our business will depend largely on future developments, including new information that may emerge concerning the severity and action taken to contain or prevent further spread within the United States and the related impact on consumer spending, all of which are highly uncertain and cannot be predicted.

Patents, Trademarks and Licenses

The Company relies on a combination of patent, trademark, and trade secret laws to establish proprietary right in its products.

We have registered the name "Electro-Sensors" as a trademark with the U.S. Patent and Trademark Office ("USPTO"), Reg. No. 1,142,310. We believe this trademark has been and will continue to be useful in developing and protecting market recognition for our products. We established the HazardPRO trademark in the first quarter of 2014 and intend to register this trademark.

We hold six patents relating to our production monitoring systems. We believe strongly in protecting our intellectual property and have a long history of obtaining patents, when available, in connection with our research and product development programs. We also rely upon trade secrets and proprietary know-how.

We seek to protect our trade secrets and proprietary intellectual property, including know-how, in part, through confidentiality agreements with employees, consultants, and other parties. We cannot ensure, however, that these agreements will not be breached, that we would have adequate remedies for any breach, or that our trade secrets will not otherwise become known or independently developed by competitors.

Seasonality

Generally, the Company experiences seasonality in the sale of its products with the second and third calendar quarters historically the strongest.

Business Development Activities

We continue to seek growth opportunities, both internally through our existing portfolio of products, technologies and markets, as well as externally through technology partnerships or related-product acquisitions. In addition, we may make investments that we believe present good opportunities for the Company and its shareholders.

Governmental Approvals

Although we are not required to obtain governmental approval of our products, we choose to obtain certain third-party certifications to meet our customers' needs. These certifications may expand our market opportunities in certain industries.

Effect of Governmental Regulations

We do not believe that, other than adjustments in tariffs imposed on imported products, any existing or proposed governmental regulations will have a material effect on our business.

Research and Development

We invest in research and development programs to develop new products and to integrate state-of-the-art technology into our existing products. We undertake development projects based upon the identified specific needs of the markets we serve. Our "Management's Discussion and Analysis of Financial Condition and Results of Operations" section describes the nature and amount of our Research and Development expenditures.

Our future success depends in part upon our ability to develop new products in our varying segments. Difficulties or delays in our ability to develop, produce, test and market new products could have a material adverse effect on future sales growth.

Compliance with Environmental Laws

Compliance with federal, state and local environmental laws has only a nominal effect on current or anticipated capital expenditures and has had no material effect on earnings or on our competitive position.

Employees

As of March 24, 2020, we had 40 employees, all of whom but one are full-time. We believe that our relations with our employees are good. None of our employees are members of unions.

Our ability to maintain a competitive position and to continue to develop and market new products depends, in part, on our ability to retain key employees and qualified personnel. If we are unable to retain our key employees, or recruit and train others, our product development, marketing and sales could be adversely affected.

Fluctuations in Operating Results

We have experienced fluctuations in our past operating results and expect to experience fluctuations in the future. These fluctuations may affect the market price of our common stock. Sales can fluctuate as a result of a variety of factors, many of which are beyond our control. These factors include: product competition and acceptance, timing of customer orders, cancellation of orders, the mix of products sold, downturns in the markets we serve and economic disruptions. Because fluctuations may occur, we caution investors that results of our operations for recent periods may not accurately predict how we will perform in the future. We cannot ensure that we will achieve revenue or earnings growth.

Expending Funds for Changes in Industry Standards, Customer Preferences or Technology

Our business depends on periodically introducing new and enhanced products and solutions for customer needs. Our product development efforts require us to commit financial resources, personnel and time, usually in advance of significant market demand for these products. In order to compete, we must anticipate both future demand and the technology available to meet that demand. We cannot ensure that our research and development efforts will lead to new products or product innovations that can be made available to or will be accepted by the market.

Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements made by us or on our behalf. We have made, and may continue to make, forward-looking statements with respect to our business and financial matters, including statements contained in this document, other filings with the Securities and Exchange Commission, and reports to shareholders. Forward-looking statements generally include discussion of current expectations or forecasts of future events and can be identified by the use of terminology such as "believe," "estimate," "expect," "intend," "may," "could," "will," and similar words or expressions. Any statement that does not relate solely to historical fact should be considered forward-looking.

Our forward-looking statements generally relate to our growth strategy, future financial results, product development and sales efforts. We make forward-looking statements throughout this Annual Report, but primarily in this Item 1 and Item 7 - *Management's Discussion and Analysis of Financial Condition and Results of Operations.* These include statements relating to our beliefs and expectations and intentions with respect to (i) our growth and profitability, (ii) our marketing and product development, (iii) the value of our intellectual property, (iv) our competitive position in the marketplace, (v) the effect of governmental regulations on our business, (vi) our employee relations, (vii) the adequacy of our facilities, (viii) our intention to develop new products, (ix) the possibility of us acquiring compatible businesses or product lines as part of our growth strategy, and (x) our future cash requirements and use of cash.

Forward-looking statements cannot be guaranteed and our actual results may vary materially due to the uncertainties and risks, known and unknown, associated with these statements, including our ability to successfully develop new products and manage our cash requirements. We undertake no obligations to update any forward-looking statements. We wish to caution investors that the following important factors, among others, in some cases have affected and in the future could affect our actual results of operations and cause these results to differ materially from those anticipated in forward-looking statements made in this document and elsewhere by us or on our behalf. We cannot foresee or identify all factors that could cause actual results to differ from expected or historical results. As such, investors should not consider any list of these factors to be an exhaustive statement of all risks, uncertainties or potentially inaccurate assumptions. These factors include our ability to:

- successfully use our cash and liquid assets to develop or acquire new or complementary products or business lines to increase our revenue and profitability;
- ensure that our operational systems, security systems and infrastructure, as well as those of third-party vendors, remain free from viruses or cyberattacks;
- quickly and successfully adapt to changing industry technological standards;
- comply with existing and changing industry regulations;
- attract and retain key personnel, including senior management;
- adapt to changing economic conditions and manage downturns or disruptions in the economy in general; including any downturns or disruptions that may result from events such as the outbreak of the COVID-19 virus; and
- keep pace with competitors, some of whom are much larger and have substantially greater resources than us.

Item 1A. Risk Factors.

This item is not required for smaller reporting companies, but above under "*Forward-Looking Statements*," we discuss some of the risk factors that are relevant to our business and operating results.

Item 2. Properties.

We own and occupy a 25,400 square foot facility at 6111 Blue Circle Drive, Minnetonka, Minnesota 55343-9108. All our operations are conducted within this facility. The facility is in excellent condition and we continue to maintain and update the facility as necessary. We believe the facility will be adequate for our needs in 2020.

Item 3. Legal Proceedings.

We are not the subject of any legal proceedings as of the date of this filing. We are not aware of any threatened litigation.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common stock trades on the Nasdaq Capital Market of The Nasdaq Stock Market® under the symbol "ELSE."

Based on data provided by our transfer agent, as of February 26, 2020, we had 67 shareholders of record who held 877,252 shares of the Company's common stock. In addition, nominees held an additional 2,518,269 shares for approximately 675 shareholders holding shares in street name.

From time to time, we may be required to repurchase some of our equity securities as a result of obligations described in Note 10 to our 2019 financial statements. We did not repurchase any equity securities during the years ended December 31, 2019 and 2018.

The information required by Item 201(d) of SEC Regulation S-K is set forth in Item 12 of this Form 10-K.

Item 6. Selected Financial Data.

Not required for smaller reporting companies

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion should be read in conjunction with our financial statements and related notes. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated due to various factors discussed under "Forward-Looking Statements" elsewhere in this Annual Report on Form 10-K.

RESULTS OF OPERATIONS

The following table contains selected financial information, for the periods indicated, from our statements of comprehensive income (loss) expressed as a percentage of net sales.

	Years Ended December 31,	
	2019	2018
Net sales	100.0%	100.0%
Cost of goods sold	47.1	46.0
Gross profit	52.9	54.0
Operating expenses		
Selling and marketing	23.4	21.8
General and administrative	20.1	23.3
Research and development	9.8	10.8
Total operating expenses	53.3	55.9
Operating loss	(0.4)	(1.9)
Non-operating income (expense)		
Interest income	2.5	1.6
Other income	0.1	0.1
Total non-operating income, net	2.6	1.7
Income (loss) before income taxes	2.2	(0.2)
Income tax benefit	0.0	(0.1)
Net income (loss)	2.2%	(0.1)%

The following paragraphs discuss the Company's performance for years ended December 31, 2019 and 2018.

Comparison of 2019 vs. 2018 (dollars in thousands)

Net Sales

Net sales for 2019 were $8,258, an increase of $763, or 10.2%, from $7,495 in 2018. The increase in net sales for the year was primarily driven by an increase in sales of our HazardPRO wireless hazard monitoring systems, which included several repeat sales to existing HazardPRO customers. Net international sales increased $139 in 2019 to 12% of total net sales. The international sales growth was led by an increase in sales to Brazil as compared to the prior year.

Gross Profit

Gross profit for 2019 increased $319, or 7.9%, to $4,366 from $4,047 in 2018. Our gross profit margin for 2019 was 52.9% compared to 54.0% in 2018. The slight decrease in the gross margin was primarily due to product mix and higher material costs resulting from the increase in United States government tariffs imposed on imported products.

Operating Expenses

Total operating expenses increased $205, or 4.9%, to $4,397 in 2019 from $4,192 in 2018, but decreased as a percentage of net sales to 53.2% from 55.9%. The increases in operating expenses was due to additional personnel and changes in internal compensation plans, partially offset by decreases in legal and professional expenses and lab testing and certification expenses.

- Selling and marketing expenses increased $295, or 18.1%, to $1,929 in 2019 from $1,634 in 2018, and increased as a percentage of net sales to 23.4% from 21.8%. The increase resulted primarily from increases in direct sales headcount and sales staff compensation due to increased net sales and changes in compensation plans.

- General and administrative expenses decreased $88, or 5.0%, to $1,657 in 2019 from $1,745 in 2018, and decreased as a percentage of net sales to 20.1% from 23.3%. The decrease was primarily due to both lower headcount and lower legal and professional expenses related to business development activities.

- Research and development expenses decreased $2, or 0.2%, to $811 in 2019 compared to $813 in 2018, and decreased as a percentage of net sales to 9.8% from 10.8%. The decrease was primarily the result of lower lab testing and certification expenses for new products.

Operating Income (Loss)

Our operating loss decreased $114 to a loss of $31 in 2019 compared to an operating loss of $145 in 2018; the operating loss improved as a percentage of net sales to -0.4% from -1.9%. The decrease was primarily related to the increase in net sales.

Non-Operating Income (Expense)

Non-operating income increased $90 to $217 in 2019 from $127 in 2018, primarily as a result of increased interest income earned from higher interest rates on Treasury Bills.

Available-for-sale equity securities are stated at fair value, and unrealized holding gains and losses are reported in our statement of comprehensive income (loss) in the non-operating income (expense) section. All other available-for-sale securities are stated at fair value, and unrealized holding gains and losses, net of the related deferred tax effect, are reported as a separate component of stockholders' equity.

Realized gains and losses, including losses from declines in value of specific securities determined by management to be other-than-temporary, are included in the statement of comprehensive income (loss). Realized gains and losses are determined on the basis of the specific securities sold.

Income Taxes

Income tax benefit was $1 in 2019 compared to $8 in 2018. The decrease was due primarily to tax credits and deferred tax adjustments. Detailed information on our income taxes are described in Note 11 to our financial statements.

Net Income (Loss)

We reported net income of $187 in 2019 compared to net loss of $10 in 2018, an increase of $197, or 1,970.0%. Basic and diluted earnings per share were $0.06 and zero in 2019 and 2018, respectively.

OFF-BALANCE SHEET ARRANGEMENTS

We are not a party to any off-balance sheet transactions, arrangements or obligations that have, or are reasonably likely to have, a material effect on our financial condition, changes in the financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents were $8,785 and $1,057 at December 31, 2019 and 2018, respectively. The increase was mainly due to net cash generated from investing activities, and the fact that at December 31, 2019, we held substantially all our available funds in assets defined as cash and cash equivalents, as described below. Working capital was $11,155 at December 31, 2019 compared to $10,942 at December 31, 2018.

Cash generated from operating activities increased $22 from $130 in 2018 to $152 in 2019. The increase was primarily due to net income in 2019 compared to a 2018 net loss and an increase in accounts payable, partially offset by an increase in trade receivables. The 2019 net income was primarily due to increased net sales. The increase in accounts payable is due to the timing of payments. The increase in trade receivables is due to the timing of sales and collections on accounts.

Cash generated from investing activities in 2019 was $7,581, compared to $115 in 2018. The increase was due to an increase in investment maturities resulting from recent Treasury Bill purchases classified as cash and cash equivalents. In addition, we purchased $257 and $32 of property, equipment, and intangibles in 2019 and 2018, respectively.

Cash used in financing activities during 2019 was $5 compared to $151 in 2018. The Company entered into a financing lease for three office copiers during 2018 reported as right-to-use assets. The lease is for 63 months with principal payments of $5 and $1 in 2019 and 2018, respectively. Detailed information on our financing lease is described in Note 8 to our 2019 financial statements. In addition, cash used in 2018 was primarily due to making the final payment on the Harvest Engineering, Inc. contingent earn-out in the 2018 first quarter.

Our ongoing cash usage requirements will be primarily used for capital expenditures, potential acquisitions, investments we believe present good opportunities for the Company and its shareholders, research and development, and working capital. 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.

CRITICAL ACCOUNTING ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make decisions based upon estimates, assumptions, and factors it considers relevant to the circumstances. Those decisions include the selection of applicable accounting principles and the use of judgment in their application, the results of which impact reported amounts and disclosures. Changes in economic conditions or other business circumstances may affect the outcomes of management's estimates and assumptions.

Significant estimates, including the underlying assumptions, consist of the economic lives of long-lived assets, realizability of trade receivables, valuation of deferred tax assets/liabilities, inventory, investments, and stock compensation expense. It is at least reasonably possible that these estimates may change in the near term.

Economic lives of long-lived assets
We estimate the economic useful life of long-lived assets used in the business. Expected asset lives may be shortened or an impairment may be recorded based on a change in the expected use of the asset. If the expected life of an asset is shortened or an impairment recorded, it could result in an additional charge to depreciation expense.

Realizability of trade receivables
We estimate our allowance for doubtful accounts based on prior history and the aging of our trade receivables. We are unable to predict which, if any, of our customers will be unable to pay their open invoices at a future date. If an account becomes uncollectible and we are required to write off the balance, we would recognize the amount of the additional expense within general and administrative expenses.

Valuation of deferred tax assets/liabilities
We estimate our deferred tax assets and liabilities based on current tax laws and rates. The tax laws and rates could change in the future to either disallow the deductions or increase/decrease the tax rates. We recognize changes in deferred tax assets and liabilities in the period in which the tax law changes become effective. Any change in our deferred tax assets or liabilities could have a material negative or positive effect on our income tax expense.

Valuation of inventory
We purchase inventory based on estimated demand of products. It is possible that the inventory we have purchased will not be used in the products that our customers need or will not meet future technological requirements. If we are unable to use the inventory in our products and it does not meet future technological requirements, we would be required to remove the items from inventory and expense the amount in cost of goods sold.

Valuation of investments
Our investments in available-for-sale securities are valued at market prices in an open market. The prices are subject to the normal fluctuations that could be either negative or positive. Changes in value of our equity securities affect our profitability as the value fluctuates. Any change in the value of our equity securities could have a material negative or positive effect on our profitability. Changes in the value of our treasury bills do not affect our profitability until the treasury bill is sold. At the time of sale, we recognize the interest earned on the treasury bill.

Valuation of stock-based compensation expense
We estimate the expected life and forfeiture rates of stock options granted when calculating the value of options using the Black-Scholes-Merton model. The actual life and forfeiture rate could differ from what we estimated. Changes in the life or forfeiture rate of stock options could have a negative or positive impact on our stock-based compensation.

Additional information regarding our significant accounting policies is provided below in Part II, Item 8, *Financial Statements and Supplementary Data – Notes to Financial Statements, Note 1, Nature of Business and Significant Accounting Policies*.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Not applicable.

Item 8. Financial Statements and Supplementary Data.

INDEX TO FINANCIAL STATEMENTS

BOULAY

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Electro-Sensors, Inc.

Opinion on the Financial Statements

We have audited the accompanying balance sheets of Electro-Sensors, Inc. (the Company) as of December 31, 2019 and 2018, and the related statements of comprehensive income (loss), changes in stockholders' equity, and cash flows for each of the years in the two-year period ended December 31, 2019, and the related notes (collectively referred to as the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2019, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Boulay PLLP
We have served as the Company's auditor since 2006.

Minneapolis, Minnesota
March 25, 2020

ELECTRO-SENSORS, INC.
BALANCE SHEETS
(in thousands except share and per share amounts)

	December 31 2019	December 31 2018
ASSETS		
Current assets		
Cash and cash equivalents	**$ 8,785**	$ 1,057
Treasury bills	**0**	7,697
Available-for-sale securities	**45**	45
Trade receivables, less allowance for doubtful accounts of $11	**1,036**	896
Inventories	**1,695**	1,618
Other current assets	**159**	155
Total current assets	**11,720**	11,468
Deferred income tax asset	**203**	192
Intangible assets, net	**489**	565
Property and equipment, net	**1,063**	1,050
Total assets	**$ 13,475**	$ 13,275
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current maturity of financing lease	**$ 5**	$ 5
Accounts payable	**129**	116
Accrued expenses	**431**	405
Total current liabilities	**565**	526
Long-term liabilities		
Financing lease, net of current maturities	**19**	24
Total long-term liabilities	**19**	24
Commitments and contingencies		
Stockholders' equity		
Common stock par value $0.10 per share; authorized 10,000,000 shares; 3,395,521 shares issued and outstanding	**339**	339
Additional paid-in capital	**2,030**	2,019
Retained earnings	**10,522**	10,335
Accumulated other comprehensive gain (unrealized gain on available-for-sale securities, net of income tax)	**0**	32
Total stockholders' equity	**12,891**	12,725
Total liabilities and stockholders' equity	**$ 13,475**	$ 13,275

See Notes to Financial Statements

ELECTRO-SENSORS, INC.
STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in thousands except share and per share amounts)

	Years ended December 31, 2019	2018
Net sales	**$ 8,258**	$ 7,495
Cost of goods sold	**3,892**	3,448
Gross profit	**4,366**	4,047
Operating expenses		
Selling and marketing	**1,929**	1,634
General and administrative	**1,657**	1,745
Research and development	**811**	813
Total operating expenses	**4,397**	4,192
Operating loss	**(31)**	(145)
Non-operating income (expense)		
Interest expense	**(2)**	(1)
Interest income	**209**	120
Other income	**10**	8
Total non-operating income, net	**217**	127
Income (loss) before income taxes	**186**	(18)
Income tax benefit	**(1)**	(8)
Net income (loss)	**187**	(10)
Other comprehensive income (loss)		
Change in unrealized value of available-for-sale securities, net of income tax	**(32)**	13
Other comprehensive income (loss)	**(32)**	13
Net comprehensive income	**$ 155**	$ 3
Net income per share data		
Basic		
Net income per share	**$ 0.06**	$ 0.00
Weighted average shares	**3,395,521**	3,395,521
Diluted		
Net income per share	**$ 0.06**	$ 0.00
Weighted average shares	**3,398,035**	3,395,521

See Notes to Financial Statements

ELECTRO-SENSORS, INC.
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(in thousands except share and per share amounts)

	Common Stock Issued		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount				
Balance, December 31, 2017	3,395,521	$ 339	$ 2,004	$ 10,352	$ 12	**$ 12,707**
Other comprehensive income					13	**13**
Stock-based compensation expense			15			**15**
Change in accounting policy				(7)	7	**0**
Net loss				(10)		**(10)**
Balance, December 31, 2018	3,395,521	339	2,019	10,335	32	**12,725**
Other comprehensive loss					(32)	**(32)**
Stock-based compensation expense			11			**11**
Net income				187		**187**
Balance, December 31, 2019	**3,395,521**	**$ 339**	**$ 2,030**	**$ 10,522**	**$ 0**	**$ 12,891**

See Notes to Financial Statements

ELECTRO-SENSORS, INC.
STATEMENTS OF CASH FLOWS
(in thousands)

	Years ended December 31, 2019	2018
Cash flows from operating activities		
Net income (loss)	**$ 187**	$ (10)
Adjustments to reconcile net income (loss) to net cash from operating activities:		
Depreciation and amortization	**320**	321
Deferred income taxes	**(2)**	(16)
Stock-based compensation expense	**11**	15
Interest accrued on treasury bills	**(182)**	(114)
Change in:		
Trade receivables	**(140)**	6
Inventories	**(77)**	(66)
Other current assets	**(4)**	(14)
Accounts payable	**13**	(62)
Accrued expenses	**26**	25
Income taxes receivable	**0**	45
Net cash from operating activities	**152**	130
Cash flows from investing activities		
Purchases of treasury bills	**(7,662)**	(14,353)
Proceeds from the maturity of treasury bills	**15,500**	14,500
Purchase of intangible asset	**(150)**	0
Purchase of property and equipment	**(107)**	(32)
Net cash from investing activities	**7,581**	115
Cash flows used in financing activities		
Payments on financing lease	**(5)**	(1)
Payment of contingent earn-out	**0**	(150)
Net cash used in financing activities	**(5)**	(151)
Net increase in cash and cash equivalents	**7,728**	94
Cash and cash equivalents, beginning	**1,057**	963
Cash and cash equivalents, ending	**$ 8,785**	$ 1,057
Supplemental cash flow information		
Cash paid during the year for income taxes	**$ 1**	$ 1
Cash paid during the year for interest	**$ 2**	$ 1
Supplemental disclosures of non-cash investment and financing activity		
Right-of-use assets obtained in exchange for finance lease obligations	$ **0**	$ 30

See Notes to Financial Statements

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2019 AND 2018
(in thousands except share and per share amounts)

Note 1. Nature of Business and Significant Accounting Policies

Nature of business:

Electro-Sensors, Inc. manufactures and markets a complete line of monitoring and control systems for a variety of industrial machinery. The Company uses leading-edge technology to continuously improve its products, with the ultimate goal of manufacturing the industry-preferred product for each market served. The Company sells these products through an internal sales staff, manufacturer's representatives, and distributors to a wide variety of industries that use the products in a variety of applications to monitor process machinery operations. The Company markets its products to customers located throughout the United States, Canada, Latin America, Europe, and Asia.

In addition, we may periodically make strategic investments in other businesses and companies, including investments that we believe would facilitate the development of new relationships, or technology complementary to our existing products, or other investments that we believe present good opportunities for the Company and its shareholders. Our primary focus is to remain an operating company and we do not intend to become an investment company. See Note 2 for additional information regarding the Company's investments. The Company's investments in securities are subject to normal market risks.

Significant accounting policies of the Company are summarized below:

Use of estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (US GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Significant estimates, including the underlying assumptions, consist of the economic lives of long-lived assets, realizability of trade receivables, valuation of deferred tax assets/liabilities, inventory, investments, stock compensation expense, and the potential estimated impact on operations due to the outbreak of the COVID-19 virus as it relates to disruptions to our supply chain and customer demand. It is at least reasonably possible that these estimates may change in the near term.

Cash and cash equivalents

The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash equivalents are invested in commercial paper, money market accounts and may, also, be invested in three-month Treasury Bills. Cash equivalents are carried at fair value.

The Company maintains its cash and cash equivalents primarily in two bank deposit accounts, which, at times, may exceed federally insured limits. The Company has not experienced any losses on these accounts. The Company believes it is not exposed to any significant credit risk on cash.

Trade receivables and credit policies

Trade receivables are uncollateralized customer obligations due under normal trade terms generally requiring payment within 30 days from the invoice date. Trade receivables are stated at the amount billed to the customer. Customer account balances with invoices over 90 days are considered delinquent. The Company does not accrue interest on delinquent trade receivables.

Payments of trade receivables are allocated to the specific invoices identified on the customer's remittance advice or, if unspecified, are applied to the earliest unpaid invoices.

The carrying amount of trade receivables is reduced by an allowance for doubtful accounts that reflects management's best estimate of the amounts that will not be collected. Management individually reviews all trade receivable balances that exceed 90 days from the invoice date and based on an assessment of current creditworthiness, estimates the portion, if any, of the balance that may not be collected. Management uses this information to estimate the allowance.

As of December 31, 2019, the Company had one customer that accounted for approximately 19% of outstanding accounts receivable. As of December 31, 2018, there was one customer that accounted for approximately 12% of the accounts receivable balance.

Available-for-sale securities

Substantially all the Company's current investments consist of government debt securities. The estimated fair value of publicly traded securities is based on reported market prices or management's reasonable market price when quoted prices are not available, and therefore subject to the inherent risk of market fluctuations.

Management determines the appropriate classification of securities at the date individual investments are acquired and evaluates the appropriateness of this classification at each balance sheet date.

Since the Company generally does not make investments in anticipation of short-term fluctuations in market price, the Company classifies its investments in equity securities and treasury bills as available-for-sale. Treasury bills 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 a separate component of stockholders' equity and within accumulated other comprehensive gain. Unrealized gains and losses on equity securities are reported in the statement of comprehensive income in non-operating income.

Realized gains and losses on securities, including losses from declines in value of specific securities determined by management to be other-than-temporary, are included in the statement of comprehensive income in non-operating income. Realized gains and losses are determined on the basis of the specific securities sold. There were no other-than-temporary impairments recognized in the years ended December 31, 2019 and 2018.

Fair value measurements

The Company's policies incorporate the guidance for accounting for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. These policies also incorporate the guidance for fair value measurement related to nonfinancial items that are recognized and disclosed at fair value in the financial statements on a nonrecurring basis. The guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.
- Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company currently has no nonfinancial or financial items that are measured on a nonrecurring basis.

The carrying value of cash equivalents, trade receivables, accounts payable, and other financial working capital items approximate fair value at December 31, 2019 and 2018 due to the short term maturity nature of these instruments.

Inventories

Inventories include material, labor and overhead and are valued at the lower of cost (first-in, first-out) or net realizable value.

Property and equipment

Property and equipment are stated at cost. Depreciation is provided over estimated useful lives by use of the straight-line method. Maintenance and repairs are expensed as incurred. Major improvements and betterments are capitalized.

Long-lived assets, such as property and equipment and intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require the Company to test a long-lived asset for possible impairment, the Company first compares undiscounted cash flows expected to be generated by an asset to the carrying value of the asset. If the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, the Company recognizes impairment to the extent that the carrying value of an asset exceeds its fair value. The Company determines fair value through various valuation techniques including, but not limited to, discounted cash flow models, quoted market values and third-party independent appraisals.

Estimated useful lives are as follows

	Years
Autos	3
Equipment	5- 10
Furniture and Fixtures	3 - 7
Building	7- 40

Intangible assets

Intangible assets are comprised of the HazardPRO technology and a communication technology. The Company amortizes the cost of these intangible assets on a straight-line method over the estimated useful lives. At December 31, 2018, the Company also had a non-compete agreement that expired in February 2019.

Revenue recognition

At contract inception, the Company assesses the goods and services promised to a customer and identifies a performance obligation for each distinct promised good or service. We also determine the transaction price for each performance obligation at contract inception. Our contracts, generally in the form of a purchase order, specify the product or service that is promised to the customer. The typical contract life is less than one month and contains a single performance obligation, to provide conforming goods or services to the customer. On some contracts, we have a second performance obligation, which typically is the initialization of the HazardPRO product. For contracts that have multiple performance obligations, we allocate the transaction price to each performance obligation using the relative stand-alone selling price. We generally determine stand-alone selling prices based on the observable stand-alone prices charged to customers. We recognize product revenue at the point in time when control of the product is transferred to the customer, which typically occurs when we ship the products. We recognize service revenue at the point in time when we have provided the service.

Advertising costs

The Company expenses advertising costs as incurred. Total advertising expense was $61 and $48 in 2019 and 2018, respectively.

Research and development

Expenditures for research and development are expensed as incurred. The Company incurred expenses of $811 and $813 in 2019 and 2018, respectively.

Income taxes

The Company presents deferred income taxes on an asset and liability approach to financial accounting and reporting for income taxes. The Company annually determines the difference between the financial reporting and tax bases of assets and liabilities. The Company computes deferred income tax assets and liabilities for those differences that have future tax consequences using the currently enacted tax laws and rates that apply to the periods in which these laws are expected to affect taxable income. Income tax expense is the current tax payable or refundable for the period plus or minus the net change in the deferred tax assets and liabilities, excluding the portion of the deferred asset or liability allocated to other comprehensive gain (loss). Deferred taxes are reduced by a valuation allowance to the extent that realization of the related deferred tax asset is not certain. We recorded a valuation allowance on our deferred tax asset of $121 and $81 at December 31, 2019 and 2018, respectively.

The Company recognizes the effect of income tax positions only if those positions are more likely than not to be sustained. The Company recognizes income tax positions at the largest amount that is more likely than not to be realized. The Company reflects changes in recognition or measurement in the period in which the Company's change in judgment occurs.

The Company records interest and penalties related to unrecognized tax benefits in income tax expense.

(in thousands except share and per share amounts)

Net income (loss) per common share

Basic earnings per share (EPS) excludes dilution and is determined by dividing net income by the weighted average number of common shares outstanding during the period. Diluted EPS reflects the potential dilution that could occur if securities such as options and other contracts to issue common stock were exercised or converted into common stock. For the years ending December 31, 2019 and 2018, respectively, options to purchase 329,986 and 332,500 weighted average common shares have been excluded from the diluted weighted average shares because their effect would be anti-dilutive.

The following information presents the Company's computations of basic and diluted EPS for the periods presented in the statements of comprehensive income (loss).

	Income (loss)	Shares	Per share amount
2019:			
Basic EPS	$ 187	3,395,521	$ 0.06
Effect of dilutive stock options		2,514	0.00
Diluted EPS	$ 187	3,398,035	$ 0.06
2018:			
Basic EPS	$ (10)	3,395,521	$ 0.00
Effect of dilutive stock options		0	0.00
Diluted EPS	$ (10)	3,395,521	$ 0.00

Stock-based compensation

The Company records compensation expense for stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes-Merton ("BSM") model. 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 December 31, 2019, the Company had two stock-based compensation plans.

Recently Adopted Accounting Pronouncements

Financial Instruments
In January 2016, the FASB issued Accounting Standards Update No. 2016-01 (ASU 2016-01) "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities," which amends various aspects of the recognition, measurement, presentation, and disclosure of financial instruments. The Company adopted ASU 2016-01 as of January 1, 2018 using the modified retrospective method for marketable equity securities. This resulted in a $7 reclassification of net unrealized losses from accumulated other comprehensive income (AOCI) to retained earnings. The adoption of ASU 2016-01 increases the possibility of increased volatility of non-operating income, as a result of the requirement to remeasure our equity securities each reporting period. For further information see Note 2.

Leases
In February 2016, the FASB issued Accounting Standards Update No. 2016-02 (ASU 2016-02) "Leases (Topic 842)" which was modified in July 2018, Accounting Standards Update No. 2018-11 (ASU 2018-11) "Leases (Topic 842): Targeted Improvements" to increase transparency and comparability among organizations by requiring the recognition of Right of Use ("ROU") assets and lease liabilities on the balance sheet. Most prominent among the changes in the standard is the recognition of ROU assets and lease liabilities by lessees for those leases classified as operating leases. Under the standard, disclosures are required to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. We elected to early adopt the standard effective October 1, 2018 in conjunction with the Company entering into a financing lease using the optional effective date method. The standard did not have a material impact in our balance sheets, statements of comprehensive income (loss), or statement of cash flows compared to the legacy accounting guidance for leases.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2019 AND 2018
(in thousands except share and per share amounts)

Note 2. Investments

The Company has investments in commercial paper, Treasury Bills, and common equity securities of a private U.S. company. The commercial paper investment is in U.S. debt with ratings of F1+. The Treasury Bills have terms ranging from one month to three months and are included within cash and cash equivalents on the balance sheet at December 31, 2019.

The Company classifies its investments in commercial paper and Treasury Bills as available-for-sale accounted for at fair value with unrealized gains and losses recognized in accumulated other comprehensive gain on the balance sheet.

Prior to January 1, 2018, the Company accounted for equity securities at fair value with unrealized gains and losses recognized in accumulated other comprehensive gain on the balance sheet. Realized gains and losses on equity securities sold or impaired were recognized in non-operating income on the statement of comprehensive loss.

On January 1, 2018, the Company adopted ASU 2016-01 which changed the way the Company accounted for equity securities. Equity securities are measured at fair value and starting January 1, 2018 unrealized gains and losses are recognized in non-operating income. Upon adoption, the Company reclassified $7 of net unrealized losses related to equity securities from accumulated other comprehensive gain to retained earnings.

The cost and estimated fair value of the investments are as follows:

	Cost	Gross unrealized gain	Gross unrealized loss	Fair value
December 31, 2019				
Commercial Paper	$ 797	$ 0	$ 0	$ 797
Treasury Bills	7,734	0	0	7,734
Equity Securities	45	0	0	45
	8,576	0	0	8,576
Less Cash Equivalents	8,531	0	0	8,531
Total Investments, December 31, 2019	$ 45	$ 0	$ 0	$ 45
December 31, 2018				
Commercial Paper	$ 667	$ 0	$ 0	$ 667
Treasury Bills	7,656	41	0	7,697
Equity Securities	45	0	0	45
	8,368	41	0	8,409
Less Cash Equivalents	667	0	0	667
Total Investments, December 31, 2018	$ 7,701	$ 41	$ 0	$ 7,742

(in thousands except share and per share amounts)

Changes in Accumulated Other Comprehensive Income

Changes in Accumulated Other Comprehensive Income are as follows:

	December 31, 2019	December 31, 2018
Unrealized Gains		
Unrealized holding gains arising during the period	**$ 0**	$ 19
Less: Reclassification of gains included in net income (loss)	**(41)**	0
	(41)	19
Deferred Taxes on Unrealized Gains:		
Increase in deferred taxes on unrealized gains arising during the period	**0**	6
Less: Reclassification of taxes on gains included in net income (loss)	**(9)**	0
	(9)	6
Net Change in Accumulated Other Comprehensive Income	**$ (32)**	$ 13

Note 3. Fair Value Measurements

The following table provides information on those assets and liabilities measured at fair value on a recurring basis.

December 31, 2019

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents:					
Commercial paper	$ 797	$ 797	$ 797	$ 0	$ 0
Treasury bills	7,734	7,734	7,734	0	0
Equity securities	45	45	0	0	45

December 31, 2018

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents:					
Commercial paper	$ 667	$ 667	$ 667	$ 0	$ 0
Treasury bills	7,697	7,697	7,697	0	0
Equity securities	45	45	0	0	45

(in thousands except share and per share amounts

The fair value of the money market funds, commercial paper, and treasury bills is based on quoted market prices in an active market. Closing prices are readily available from active markets and are used as being representative of fair value. The Company classifies these securities as level 1. The only equity security owned by the Company is an investment in a limited-marketable company. There is an insignificant market for this limited-marketable company and the Company has determined the value based on financial and other factors, which are considered level 3 inputs in the fair value hierarchy.

The change in level 3 assets at fair value on a recurring basis is summarized as follows:

	Years Ended December 31,	
	2019	**2018**
Beginning Balance	**$ 45**	$ 45
Change in value	**0**	0
Ending Balance	**$ 45**	$ 45

The change in level 3 liabilities at fair value on a recurring basis is summarized as follows:

	Year Ended December 31, 2018
Beginning Balance	$ 150
Credit to Earnings	0
Payments	(150)
Ending Balance	$ 0

The 2018 decrease reflects the final payment of the liability according to the terms of the underlying agreement. No liability exists at December 31, 2019.

(in thousands except share and per share amounts

Note 4. Inventories

Inventories used in the determination of cost of goods sold are as follows:

	December 31, 2019	December 31, 2018
Raw Materials	**$ 973**	$ 968
Work In Process	**383**	309
Finished Goods	**359**	351
Reserve for Obsolescence	**(20)**	(10)
Total Inventories	**$ 1,695**	$ 1,618

Note 5. Property and Equipment, Net

The following is a summary of property and equipment:

	December 31, 2019	December 31, 2018
Autos	**$ 23**	$ 0
Equipment	**308**	274
Furniture and Fixtures	**526**	503
Right-of-Use Asset	**30**	30
Building	**1,378**	1,370
Land	**415**	415
	2,680	2,592
Less Accumulated Depreciation	**1,617**	1,542
Total Property and Equipment	**$ 1,063**	$ 1,050

Depreciation expense for the years ended December 31, 2019 and 2018 was $94 and $86, respectively.

(in thousands except share and per share amounts)

Note 6. Net Intangible Assets

Intangible assets include the following:

		December 31, 2019		
	Average Useful Lives	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Non-compete	5 Years	$ 120	$ 120	$ 0
Technology	7 Years	1,478	1,126	352
Communication Technology	3 Years	150	13	137
Net Intangible Assets		$ 1,748	$ 1,259	$ 489

		December 31, 2018		
	Average Useful Lives	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Non-compete	5 Years	$ 120	$ 118	$ 2
Technology	7 Years	1,478	915	563
Net Intangible Assets		$ 1,598	$ 1,033	$ 565

Amortization expense for the years ended December 31, 2019 and 2018 was $226 and $235, respectively.

Estimated amortization expense over the next three years is as follows:

2020	$ 261
2021	$ 191
2022	$ 37

Note 7. Accrued Expenses

Accrued expenses include the following:

	December 31,	
	2019	2018
Wages and Commissions	**$ 359**	$ 326
Other	**72**	79
Total Accrued Expenses	**$ 431**	$ 405

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2019 AND 2018
(in thousands except share and per share amounts)

Note 8. Leases

The Company has a financing lease for office equipment. The lease has a remaining term of four years at December 31, 2019.

The components of lease expense were as follows:

	Years Ended December 31, 2019	Years Ended December 31, 2018
Finance lease cost:		
Amortization of right-of-use assets	$ 6	$ 2
Interest on lease liabilities	2	1
Total finance lease cost	$ 8	$ 3

Supplemental balance sheet information related to leases is as follows:

	December 31, 2019	December 31, 2018
Finance leases		
Property and equipment, gross	$ 30	$ 30
Accumulated amortization	(7)	(2)
Property and equipment, net	$ 23	$ 28

Weighted average remaining lease term	
Finance leases	4 years
Weighted average discount rate	
Finance leases	7.0%

Maturities of lease liabilities are as follows:

Year ending December 31	
2020	$ 7
2021	7
2022	7
2023	6
Total lease payments	27
Less imputed interest	(3)
Total	$ 24

(in thousands except share and per share amounts)

Note 9. Common Stock Options

Stock options

The 1997 Stock Option Plan (the “1997 Plan”) and 2013 Equity Incentive Plan (the “2013 Plan”) authorize the issuance of both nonqualified and incentive stock options. Payment for the shares may be made in cash, shares of the Company’s common stock or a combination thereof. Under the terms of the plans, incentive stock options and non-qualified stock options are granted at a minimum of 100% of fair market value on the date of grant and may be exercised at various times depending upon the terms of the option. All existing options expire 10 years from the date of grant or one year from the date of death.

Stock-based compensation

Under the 2013 Plan, the Company is authorized to grant options to purchase up to 600,000 shares of its common stock. As of December 31, 2019, options to purchase an aggregate of 325,000 shares were outstanding under the 2013 Plan, of which options to purchase 300,000 shares were exercisable, and 275,000 additional shares were available for issuance pursuant to awards that may be granted under the plan in the future.

Under the 1997 Plan, the Company was authorized to grant options to purchase up to 450,000 shares of its common stock. As of December 31, 2019, options to purchase an aggregate of 7,500 shares were outstanding and exercisable under the 1997 Plan. The board terminated the plan in 2014. The existing grants may be exercised according to the terms of the grant agreements.

There were no options granted during 2019.

During the 2018 fourth quarter, the Company granted an employee options to purchase 25,000 shares of common stock. The options were priced at fair market value and vested 20% on the grant date, with an additional 20% vesting on the first four anniversaries of the grant date. The options expire 10 years from the date of grant.

The assumptions made in estimating the fair value of the options on the grant date based upon the BSM option-pricing model for the year ended December 31, 2018 are as follows:

Dividend Yield	0.00%
Expected Volatility	18.79%
Risk Free Interest Rate	3.03%
Expected Life	6 Years

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

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2019 AND 2018
(in thousands except share and per share amounts)

The following table summarizes the activity for outstanding incentive stock options under the 2013 Plan to employees of the company:

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (1)
Balance at January 1, 2018	100,000	$ 3.81	7.7	
Granted	25,000	3.64	10.0	
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2018	125,000	3.78	8.1	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2019	125,000	$ 3.78	7.1	
Vested and exercisable as of December 31, 2019	100,000			$ 9

(1) The aggregate intrinsic value is calculated as approximately the difference between the weighted average exercise price of the underlying awards and the Company's estimated current fair market value at December 31, 2019.

The following table summarizes the activity for outstanding stock options under the 2013 Plan and 1997 Plan to directors of the company:

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (1)
Balance at January 1, 2018	207,500	$ 4.62	5.4	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2018	207,500	4.62	4.4	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2019	207,500	$ 4.62	3.4	
Vested and exercisable as of December 31, 2019	207,500			$ 0

(1) The aggregate intrinsic value is calculated as approximately the difference between the weighted average exercise price of the underlying awards and the Company's estimated current fair market value at December 31, 2019.

The weighted average grant date fair value of options granted during the year ended December 31, 2018, under the 2013 Plan, was $3.64. The Company recognized compensation expense in connection with the issuance of the options of approximately $11 and $15 during the years ended December 31, 2019 and 2018, respectively.

There were no options exercised during the years ended December 31, 2019 and 2018.

As of December 31, 2019, there was approximately $15 of unrecognized compensation expense under the 2013 Plan. The Company expects to recognize this expense over the next three years. To the extent the forfeiture rate is different than we have anticipated; stock-based compensation related to these awards will be different from our expectations.

Note 10. Benefit Plans

Employee stock ownership plan

The Company sponsors an employee stock ownership plan (“ESOP”) that covers substantially all employees who work 1,000 or more hours during the year. The ESOP has, at various times, secured financing from the Company to purchase the Company’s shares on the open market. When the ESOP purchases shares with the proceeds of the Company loans, the shares are pledged as collateral for these loans. The shares are maintained in a suspense account until released and allocated to participant accounts. The ESOP owns 135,490 shares of the Company’s stock at December 31, 2019. All shares held by the ESOP have been released and allocated to participants' accounts. No dividends were paid during the years ended December 31, 2019 and 2018. The ESOP had no debt to the Company at December 31, 2019 or 2018.

The Company recognized compensation expense for contributions of $24 to the ESOP plan in both 2019 and 2018.

In the event a terminated ESOP participant desires to sell his or her shares of the Company’s stock and the shares are not readily tradable, the Company may be required to purchase the shares from the participant at fair market value. In addition, at its election, the Company may distribute the ESOP’s shares to the terminated participant. At December 31, 2019, 135,490 shares of the Company’s stock, with an aggregate fair market value of approximately $492, are held by ESOP participants who, if terminated, would have rights under the repurchase provisions if the Company's stock were not readily traded. The Company believes that the market for its shares meets the ESOP requirements and that there would not be a current obligation to repurchase shares.

Profit sharing plan and savings plan

The Company has a salary reduction and profit sharing plan that conforms to IRS provisions for 401(k) plans. The Company may make profit-sharing contributions with the approval of the Board of Directors. There were no profit-sharing contributions by the Company in 2019 or 2018.

(in thousands except share and per share amounts)

Note 11. Income Taxes

The components of the income tax provision for the years ended December 31, 2019 and 2018 are as follows:

	2019	2018
Current:		
Federal	$ **0**	$ 0
State	**1**	1
Deferred:		
Federal	**(2)**	(9)
State	**0**	0
Total Federal and State Income Taxes	$ **(1)**	$ (8)

The provision for income taxes for the years ended December 31, 2019 and 2018 differs from the amount obtained by applying the U.S. federal income tax rate to pretax income due to the following:

	2019	2018
Computed "Expected" Federal Tax Expense (Benefit From)	**$ 39**	$ (4)
Increase (Decrease) in Taxes Resulting From:		
State Income Taxes, net of Federal Benefit	**1**	1
R&D Credits	**(72)**	(41)
Permanent Differences	**5**	7
Other	**26**	29
Total Federal and State Income Taxes	**$** **(1)**	$ (8)

(in thousands except share and per share amounts)

The components of the net deferred tax asset consist of:

	2019	2018
Deferred Tax Assets:		
Vacation accrual	**$ 24**	$ 24
Allowance for doubtful accounts	**2**	2
Stock compensation	**93**	91
Bonus	**2**	0
Depreciation and amortization	**50**	29
Inventory Obsolescence	**4**	2
R&D credit carryforward	**171**	154
Valuation allowance	**(121)**	(81)
Total Deferred Tax Assets	**225**	221
Deferred Tax Liabilities:		
Prepaid expenses	**22**	20
Net unrealized gain on investments	**0**	9
Total Deferred Tax Liabilities	**22**	29
Net Deferred Tax Asset	**$ 203**	$ 192

The Company is materially subject to the following taxing jurisdictions: U.S. and Minnesota. The tax years 2016 through 2018 remain open to examination by the Internal Revenue Service and state jurisdictions. We have no accrued interest or penalties related to uncertain tax positions as of January 1, 2019 or December 31, 2019 and uncertain tax positions are not significant.

Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The person serving as our principal executive officer and principal financial officer evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act"). Based on this evaluation, the person serving as the Company's principal executive officer and principal financial officer has concluded that the Company's disclosure controls and procedures were effective as of December 31, 2019 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control over Financial Reporting

Under Section 404 of the Sarbanes-Oxley Act of 2002, our management is required to assess the effectiveness of the Company's internal control over financial reporting as of the end of each fiscal year and report, based on that assessment, whether the Company's internal control over financial reporting is effective.

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control over financial reporting is designed to provide reasonable assurance as to the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Internal control over financial reporting, no matter how well designed, has inherent limitations. Therefore, internal control over financial reporting determined to be effective can provide only reasonable assurance with respect to financial statement preparation and may not prevent or detect all misstatements. Moreover, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management has assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2019. In making this assessment, the Company used the criteria established by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in "*Internal Control-Integrated Framework (2013)*." These criteria are in the areas of control environment, risk assessment, control activities, information and communication, and monitoring. The Company's assessment included extensive documenting, evaluating and testing the design and operating effectiveness of its internal control over financial reporting. Based on this evaluation, the person serving as the Company's principal executive officer and principal financial officer has concluded that the Company's internal controls were effective as of December 31, 2019.

Changes in Internal Control over Financial Reporting

There have been no changes in the Company's internal control over financial reporting that occurred during the fourth quarter of fiscal year 2019, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information.

None

PART III

Certain information required by Part III is incorporated by reference to the Company's Definitive Proxy Statement pursuant to Regulation 14A (the "2020 Proxy Statement") for its Annual Meeting of Shareholders to be held April 22, 2020 ("Annual Meeting").

Item 10. Directors, Executive Officers and Corporate Governance.

The information required by Item 401 under Regulation S-K, to the extent applicable to the Company's directors, will be set forth under the caption "Election of Directors" in the 2020 Proxy Statement and is incorporated herein by reference. The information required with respect to the Company sole executive officer, who is also a director, will be set forth under the caption "Election of Directors."

The information required by Item 405 regarding compliance with Section 16(a) will be set forth under the caption "Delinquent Section 16(a) Reports" in the 2020 Proxy Statement and is incorporated herein by reference.

Code of Ethics and Business Conduct

The Company has adopted the Electro-Sensors Code of Ethics and Business Conduct (the "Code of Conduct") applicable to all officers and employees of the Company. A copy of the Code of Conduct can be obtained free of charge upon written request directed to the Company's Chief Executive Officer at the Company's executive offices. Any amendment to, or waiver from, a provision of our Code of Conduct will be posted to our website.

The information required by Item 407 regarding corporate governance will be set forth under the caption "Corporate Governance" in the 2020 Proxy Statement and is incorporated herein by reference.

Item 11. Executive Compensation.

The information called for by Item 402 under Regulation S-K, will be set forth under the caption "Executive Compensation" in the Company's 2020 Proxy Statement and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information called for by Item 403 under Regulation S-K will be set forth under the caption "Security Ownership of Certain Beneficial Owners and Management" in the Company's 2020 Proxy Statement and is incorporated herein by reference.

The following table provides information as of December 31, 2019 about the Company’s equity compensation plans.

Equity Compensation Plan Information

	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	**(b)**	**(c)**
Equity compensation plans approved by security holders	332,500	$4.30	275,000[1]
Equity compensation plans not approved by security holders	—	—	—
Total	332,500	$4.30	275,000[1]

[1] Shares issuable pursuant to the 2013 Equity Incentive Plan.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by Item 404 under Regulation S-K will be set forth under the caption “Transactions with Related Persons, Promoters and Certain Control Persons” in the 2020 Proxy Statement and is incorporated herein by reference.

The information required by Item 407(a) will be set forth in the 2020 Proxy Statement under the caption “Corporate Governance” and is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services.

The information required by Item 14 of Form 10-K and 9(e) of Schedule 14A will be set forth under the caption “Ratification of Independent Registered Public Accounting Firm” in the Company’s 2020 Proxy Statement and is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

Financial Statements.

Reference is made to the Index to Financial Statements appearing on Page 14 hereof.

Financial Statement Schedules.

The Financial Statement Schedules have been omitted either because they are not required or because the information has been included in the financial statements or the notes thereto included in this Annual Report.

Exhibits.

Exhibit Number	Exhibit Description
3.1	Registrant's Restated Articles of Incorporation, as amended—incorporated by reference to Exhibit 3.1 to the Company's 1991 Form 10-KSB
3.2	Registrant's Bylaws, as amended to date—incorporated by reference to Exhibit 3.2 to the Company's 1997 Form 10-KSB
4.1	Description of the Registrant's Securities Registered Pursuant to Section 12 of the Securities Exchange Act of 1934
*10.1	Electro-Sensors, Inc. 1997 Stock Option Plan —incorporated by reference to Exhibit 10.6 to the Company's 1997 Form 10-KSB
*10.2	Electro-Sensors, Inc. 2013 Equity Incentive Plan incorporated by reference to Appendix A of the Company's Proxy Statement for the Company's 2016 Annual Meeting of Shareholders
*10.4	Form of Incentive Stock Option Agreement under the 2013 Equity Incentive Plan – incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on April 29, 2013
*10.5	Form of Non-qualified Stock Option Agreement under the 2013 Equity Incentive Plan – incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on April 29, 2013
23.1	Consent of Independent Registered Public Accounting Firm
24.1	Power of Attorney (see Signature page)
31.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.1	Letter to Shareholders dated March 25, 2020
99.2	Investor Information
101	The following financial information from Electro-Sensors, Inc.'s Annual Report on Form 10-K for the annual period ended December 31, 2019, formatted in iXBRL (Inline eXtensible Business Reporting Language): (i) Balance Sheets as of December 31, 2019 and 2018, (ii) Statements of Comprehensive Income (Loss) for the years ended December 31, 2019 and 2018, (iii) Statements of Cash Flows for years ended December 31, 2019 and 2018, (iv) Statement of Changes in Stockholders' Equity, and (v) Notes to Financial Statements.

* Incorporated by reference to a previously filed report or document—SEC File No. 000-09587

* Management contract or compensatory plan or arrangement

Item 16. Form 10K Summary

None

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.

ELECTRO-SENSORS, INC.
("Registrant")
By: /s/ DAVID L. KLENK
David L. Klenk
President, Chief Executive Officer, and Chief Financial Officer
Date: March 25, 2020

By: /s/ GLORIA M. GRUNDHOEFER
Gloria M. Grundhoefer
Controller
Date: March 25, 2020

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

(Power of Attorney)

Each person whose signature appears below constitutes and appoints DAVID L. KLENK as his true and lawful attorney-in-fact and agent, with full power of substitution and re-substitution, for him and in his name, place and stead, in any and all capacities, to sign any or all amendments to this Annual Report on Form 10-K and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all said attorney-in-fact and agents, or his substitute or substitutes, may lawfully do or cause to be done by virtue thereof.

Signature	**Title**	**Date**
/s/David L. Klenk	President and Director (CEO and CFO)	March 25, 2020
/s/ Joseph A. Marino	Chairman and Director	March 25, 2020
/s/ Scott A. Gabbard	Director	March 25, 2020
/s/ Michael C. Zipoy	Director	March 25, 2020
/s/ Jeffrey D. Peterson	Director	March 25, 2020

Exhibit 4.1

**DESCRIPTION OF THE REGISTRANT'S SECURITIES
REGISTERED PURSUANT TO SECTION 12 OF THE
SECURITIES EXCHANGE ACT OF 1934**

Electro-Sensors, Inc. ("ELSE," "we," "our," or "us") has one class of securities registered under Section 12 of the Securities Exchange Act of 1934, as amended: our common stock.

DESCRIPTION OF CAPITAL STOCK

The following summary of the general terms and provisions of our capital stock does not purport to be complete and is based upon and qualified by reference to our articles of incorporation and bylaws, which are available from the Company and are incorporated by reference herein. We encourage you to read our articles of incorporation, our bylaws and the applicable provisions of the Minnesota Business Corporation Act, or MBCA, for additional information.

Authorized Shares of Capital Stock

The aggregate number of shares of capital stock that the Company has authority to issue is 10,000,000 shares of common stock, par value $.10.

Common Stock

Holders of the Company's common stock are entitled to one vote for each share held of record on all matters submitted to a vote of the shareholders and do not have cumulative voting rights. Except as otherwise provided by law, our articles of incorporation or our bylaws, matters will generally be decided by the vote of the holders of a majority of the voting power present in person or represented by proxy. Our bylaws provide that the authorized number of directors will be fixed by the shareholders at each annual meeting and that either the shareholders or the board of directors may increase or decreases the number of directors. Our board of directors is not classified.

Holders of our common stock are entitled to receive dividends declared by our board of directors out of funds legally available for the payment of dividends. In the event of any liquidation, dissolution or winding-up of our affairs, holders of common stock will be entitled to share ratably in our assets that are remaining after payment or provision for payment of all of our debts and obligations.

Holders of common stock have no preemptive, conversion or subscription rights, and there are no redemption provisions applicable to the common stock.

All outstanding shares of our common stock are fully paid and nonassessable.

The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company, Corporate Trust Services, 6201 15th Avenue, Brooklyn, NY 11219

Our common stock is currently listed on The NASDAQ Stock Market LLC under the trading symbol "ELSE."

Preferred Stock

We have no preferred stock authorized or outstanding.

Anti-Takeover Effects of Provisions of our Articles of Incorporation, our Bylaws and Minnesota Law

Specific provisions of Minnesota law, our articles of incorporation and our bylaws may be deemed to have an anti-takeover effect.

Shareholder Meetings

Under our bylaws, annual meetings of our shareholders may be called only by our board of directors, or by written consent of all the shareholders entitled to vote at the annual meeting.

Under our bylaws, special meetings of our shareholders may be called by the Secretary upon request of the Chairman, the President or the board of directors (acting by majority vote), or by a shareholder or shareholders holding 10% or more of the voting power of the shareholders.

Unanimous Shareholder Action in Writing

Our bylaws permit shareholders to take any action that might be taken at a meeting of the shareholders by written action, but only if it is signed by all of the shareholders entitled to vote on that action.

Provisions of Minnesota Law

The following provisions of the MBCA may have an effect of delaying, deterring or preventing an unsolicited takeover of the Company or make an unsolicited takeover of the Company more difficult.

MBCA Section 302A.553 [**Power to acquire shares]** subd 3, **[limitation on share purchases]** prohibits a publicly held corporation such as ELSE from purchasing shares entitled to vote for more than market value from a person that beneficially owns more than 5% of the voting power of the corporation if the shares have been beneficially owned for less than two years unless the purchase or agreement to purchase is approved at a meeting of shareholders by the affirmative vote of the holders of a majority of the voting power of all shares entitled to vote or the corporation makes an offer, of at least equal value per share, to all shareholders for all other shares of that class or series and any other class or series into which they may be converted.

MBCA Section 302A.671 [**Control share acquisitions]** provides that shares of an "issuing public corporation," such as ELSE, acquired by an "acquiring person" in a "control share acquisition" that exceed the threshold of voting power of any of the three ranges identified below will not have voting rights, unless the issuing public company's shareholders vote to accord these shares the voting rights normally associated with these shares. A "control share acquisition" is an acquisition, directly or indirectly, by an "acquiring person" (as defined in the MBCA) of beneficial ownership of shares of an issuing public corporation that, but for Section 302A.671, would, when added to all other shares of the issuing public corporation beneficially owned by the acquiring person, entitle the acquiring person, immediately after the acquisition, to exercise or direct the exercise of a new range of voting power of the issuing public corporation with any of the following three ranges: (i) at least 20 percent but less than 33-1/3 percent; (ii) at least 33-1/3 percent but less than or equal to 50 percent; and (iii) over 50 percent. The issuing public company also has an option to call for redemption all, but not less than all, shares acquired in the control share acquisition that exceed the threshold of voting power of any of the specified ranges at a price equal to the fair market value of the shares at the time the call is given if (i) the acquiring person fails to deliver the information statement to the issuing public company by the tenth day after the control share acquisition; or (ii) shareholders have voted not to accord voting rights to the shares acquired in the control share acquisition.

Note: The Company amended its articles in 1991 to provide that MBCA Section 302A.671 does not apply to the Company.

MBCA Section 302A.673 [**Business combinations]** prohibits a public Minnesota corporation, such as ELSE, from engaging in a business combination with an interested shareholder for a period of four years after the date of the transaction in which the person became an interested shareholder, unless either (i) the business combination or (ii) the acquisition by which the person becomes an interested shareholder is approved in a prescribed manner before the person became an interested shareholder. The term "business combination" includes mergers, asset sales and other transactions resulting in a financial benefit to the interested shareholder. An "interested shareholder" is a person who is the beneficial owner, directly or indirectly, of 10% or more of a corporation's voting stock, or who is an affiliate or associate of the corporation, and who, at any time within four years before the date in question, was the beneficial owner, directly or indirectly, of 10% or more of the corporation's outstanding voting stock.

If a takeover offer is made for our stock, MBCA Section 302A.675 [**Takeover offer; fair price]** precludes the offeror from acquiring additional shares of stock (including in acquisitions pursuant to mergers, consolidations or statutory share exchanges) within two years following the completion of the takeover offer, unless shareholders selling their shares in the later acquisition are given the opportunity to sell their shares on terms that are substantially the same as those contained in the earlier takeover offer. A "takeover offer" is a tender offer that results in an offeror who owned ten percent or less of a class of our shares acquiring more than ten percent of that class, or that results in the offeror increasing its beneficial ownership of a class of our shares by more than ten percent of the class, if the offeror owned ten percent or more of the class before the takeover offer. Section 302A.675 does not apply if a committee of our board of directors formed in accordance with Section 302A.675 approves the proposed acquisition before any shares are acquired pursuant to the earlier tender offer.

EXHIBIT 23.1

BOULAY

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements on Form S-8 (333-48995 and 333-210944) of Electro-Sensors, Inc. of our report dated March 25, 2020 relating to the financial statements that appear in this Annual Report on Form 10-K for the year ended December 31, 2019.

/s/ Boulay PLLP
Minneapolis, MN
March 25, 2020

EXHIBIT 31.1

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES OXLEY-ACT OF 2002

I, David L. Klenk, certify that:

1. I have reviewed this report on Form 10-K of Electro-Sensors Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the registrant is made known to me by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under my supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

March 25, 2020

/s/ David L. Klenk

David L. Klenk
Chief Executive Officer and Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Electro-Sensors, Inc. (the "Company") on Form 10-K for the year ended December 31, 2019 as filed with the Securities and Exchange Commission (the "Report"), I, David L. Klenk, Chief Executive Officer and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

March 25, 2020

/s/ David L. Klenk

David L. Klenk

Chief Executive Officer and Chief Financial Officer

Exhibit 99.1

March 25, 2020

Dear Shareholders:

It has certainly been an exciting year for us as we've carried out our mission of providing industry leading machine monitoring sensors and hazard monitoring systems to industrial and agricultural customers around the world. While many things have changed in our business over the last 50-plus years, our passion for serving customers has never wavered as we work to keep our customers' people safe and their plants running efficiently.

We are pleased to announce we achieved record annual revenue in 2019 of over $8.2 million, an increase of 10% over prior-year results. International sales remain an important part of our business and delivered approximately 12% of our revenues. Gross profit for the year was 53%, driven by our continued focus on manufacturing efficiencies and cost controls. While the ever-changing tariff situation added increased drama to our operations, I'm proud of our team for working closely with our supply chain to maintain a steady flow of components used in our manufacturing process.

Our revenue growth was primarily driven by increased sales of our HazardPRO™ wireless hazard monitoring systems. These systems are the clear industry leader for wirelessly monitoring critical automation processes, while providing an exceptional overall value to our customers. We were particularly excited to receive several repeat and multi-system HazardPRO orders as customers outfit additional facilities with the proven technology.

Furthermore, we continue to develop our systems and technologies to best position us for the future. The industrial demand for process knowledge continues to expand and we believe we are in the right place at the right time to meet many of these emerging needs. We have a focused technology roadmap that will allow us to expand into even more industrial applications and provide our customers with real-time information to optimize their operations.

As you might have guessed, all these dynamics make it a very interesting time to be a sensor and process monitoring company. The challenge before us now is to build upon our strong foundation as we become an increasingly important player in the machine monitoring and hazard monitoring markets. Our team is eager and ready to take on this challenge as we drive Electro-Sensors forward.

And finally, we need to acknowledge that 2020 is going to be a challenging year as the nation and world contend with the COVID-19 virus. Our first priority is the safety and health of our employees, followed by our enduring commitment to support our customers as they provide critical food, medical and industrial supplies that will help get us through this challenging time.

Thanks again for your interest and support of Electro-Sensors. We look forward to seeing you at our annual shareholder meeting later this year. We will publish the date and time of the meeting in our upcoming proxy statement as well as on our website (www.electro-sensors.com).

Sincerely,

David Klenk

Exhibit 99.2

INVESTOR INFORMATION

Annual Meeting

The date and location of our Annual Meeting of Shareholders will be announced at a later date via the proxy statement and on our corporate website (www.electro-sensors.com). All shareholders are welcome to attend and take part in the discussion of Company affairs.

Board of Directors
David L. Klenk
President, Electro-Sensors, Inc.

Joseph A. Marino
Chairman of the Board
President, Cardia, Inc.

Scott A. Gabbard
CFO, Magenic Technologies, Inc.

Michael C. Zipoy
Retired Investment Executive, Feltl and Company

Jeffrey D. Peterson
Private Investor

Officers
David L. Klenk
President, Chief Executive Officer and Chief Financial Officer

Transfer Agent & Registrar
American Stock Transfer & Trust Company
Corporate Trust Services
6201 15th Avenue
Brooklyn, NY 11219

Auditors
Boulay P.L.L.P.
7500 Flying Cloud Drive, Ste. 800
Minneapolis, MN 55344

Counsel
Ballard Spahr LLP
2000 IDS Center
80 South Eighth Street
Minneapolis, MN 55402-2274

Exchange Listing
The Nasdaq Stock Market (Capital Market)
Common Stock
Stock Trading Symbol: **ELSE**