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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549**

**Form 10-Q**

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

**For the quarterly period ended March 31, 2020**

**Or**

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

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

**Commission File Number 000-09587**

**ELECTRO-SENSORS, INC.**

(Exact name of registrant as specified in its charter)

**Minnesota**

(State or other jurisdiction of incorporation or  
organization)

**41-0943459**

(IRS Employer Identification No.)

**6111 Blue Circle Drive  
Minnetonka, Minnesota 55343-9108**

(Address of principal executive offices)

**(952) 930-0100**

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol(s) | Name of each exchange on which<br>registered |
|---------------------|-------------------|--|
| Common stock        | ELSE              | Nasdaq Capital Market                        |

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 ☐

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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 ☐

Non-accelerated filer ☐

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 number of shares outstanding of the registrant's common stock, \$0.10 par value, on May 8, 2020 was 3,395,521.

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**ELECTRO-SENSORS, INC.**  
**Form 10-Q**  
**For the Periods Ended March 31, 2020**

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## PART I. FINANCIAL INFORMATION

### Item 1. Financial Statements

#### ELECTRO-SENSORS, INC. CONDENSED BALANCE SHEETS

(in thousands except share and per share amounts)

|  | March 31,<br>2020 | December 31,<br>2019 |
|--|-------------------|----------------------|
|  | (unaudited)       |                      |
| <b>ASSETS</b>  |                   |                      |
| <b>Current assets</b>  |                   |                      |
| Cash and cash equivalents  | \$ 7,850          | \$ 8,785             |
| Investments  | 1,041             | 45                   |
| Trade receivables, less allowance for doubtful accounts of \$11  | 934               | 1,036                |
| Inventories  | 1,721             | 1,695                |
| Other current assets   | 204               | 159                  |
| Income tax receivable  | 15                | 0                    |
| <b>Total current assets</b>  | <b>11,765</b>     | <b>11,720</b>        |
| <b>Deferred income tax asset, net</b>  | <b>207</b>        | <b>203</b>           |
| <b>Intangible assets, net</b>  | <b>424</b>        | <b>489</b>           |
| <b>Property and equipment, net</b>   | <b>1,038</b>      | <b>1,063</b>         |
| <b>Total assets</b>  | <b>\$ 13,434</b>  | <b>\$ 13,475</b>     |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                   |                      |
| <b>Current liabilities</b>   |                   |                      |
| Current maturities of financing lease  | \$ 6              | \$ 5                 |
| Accounts payable   | 198               | 129                  |
| Accrued expenses   | 411               | 431                  |
| <b>Total current liabilities</b>   | <b>615</b>        | <b>565</b>           |
| <b>Long-term liabilities</b>   |                   |                      |
| Financing lease, net of current maturities   | 16                | 19                   |
| <b>Total long-term liabilities</b>   | <b>16</b>         | <b>19</b>            |
| <b>Commitments and contingencies</b>   |                   |                      |
| <b>Stockholders' equity</b>  |                   |                      |
| 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   | 2,033             | 2,030                |
| Retained earnings  | 10,431            | 10,522               |
| <b>Total stockholders' equity</b>  | <b>12,803</b>     | <b>12,891</b>        |
| <b>Total liabilities and stockholders' equity</b>  | <b>\$ 13,434</b>  | <b>\$ 13,475</b>     |

See accompanying notes to unaudited condensed financial statements

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

|  | Three Months Ended<br>March 31, |                 |
|--|---------------------------------|-----------------|
|  | 2020                            | 2019            |
| <b>Net sales</b>   | <b>\$ 1,923</b>                 | <b>\$ 2,008</b> |
| <b>Cost of goods sold</b>  | <b>924</b>                      | <b>941</b>      |
| <b>Gross profit</b>  | <b>999</b>                      | <b>1,067</b>    |
| <b>Operating expenses</b>  |                                 |                 |
| Selling and marketing  | 458                             | 485             |
| General and administrative   | 465                             | 472             |
| Research and development   | 217                             | 196             |
| <b>Total operating expenses</b>  | <b>1,140</b>                    | <b>1,153</b>    |
| <b>Operating loss</b>  | <b>(141)</b>                    | <b>(86)</b>     |
| <b>Non-operating income (expense)</b>  |                                 |                 |
| Loss on investment   | (3)                             | 0               |
| Interest income  | 32                              | 44              |
| Other income   | 2                               | 2               |
| <b>Total non-operating income, net</b>   | <b>31</b>                       | <b>46</b>       |
| <b>Loss before income tax benefit</b>  | <b>(110)</b>                    | <b>(40)</b>     |
| <b>Benefit from income tax</b>   | <b>(19)</b>                     | <b>(9)</b>      |
| <b>Net loss</b>  | <b>\$ (91)</b>                  | <b>\$ (31)</b>  |
| <b>Other comprehensive income</b>  |                                 |                 |
| Change in unrealized value of available-for-sale securities, net of income tax | \$ 0                            | \$ 1            |
| <b>Other comprehensive income</b>  | <b>0</b>                        | <b>1</b>        |
| <b>Net comprehensive loss</b>  | <b>\$ (91)</b>                  | <b>\$ (30)</b>  |
| <b>Net loss per share data:</b>  |                                 |                 |
| <b>Basic</b>   |                                 |                 |
| Net loss per share   | \$ (0.03)                       | \$ (0.01)       |
| Weighted average shares  | 3,395,521                       | 3,395,521       |
| <b>Diluted</b>   |                                 |                 |
| Net loss per share   | \$ (0.03)                       | \$ (0.01)       |
| Weighted average shares  | 3,395,521                       | 3,395,521       |

See accompanying notes to unaudited condensed financial statements

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

**For the three months ended March 31**

|   | Common Stock<br>Issued  |                      | Additional<br>Paid-in<br>Capital | Retained<br>Earnings    | Accumulated<br>Other<br>Comprehensive<br>Income | Total<br>Stockholders'<br>Equity |
|---|-------------------------|----------------------|----------------------------------|-------------------------|---|----------------------------------|
|   | Shares                  | Amount               |                                  |                         |   |                                  |
| December 31, 2019                             | 3,395,521               | \$ 339               | \$ 2,030                         | \$ 10,522               | \$ 0  | \$ 12,891                        |
| Stock-based compensation expense              |                         |                      | 3                                |                         |   | 3                                |
| Net loss                                      |                         |                      |                                  | (91)                    |   | (91)                             |
| <b>Balance March 31, 2020<br/>(unaudited)</b> | <b><u>3,395,521</u></b> | <b><u>\$ 339</u></b> | <b><u>\$ 2,033</u></b>           | <b><u>\$ 10,431</u></b> | <b><u>\$ 0</u></b>                              | <b><u>\$ 12,803</u></b>          |
| December 31, 2018                             | 3,395,521               | \$ 339               | \$ 2,019                         | \$ 10,335               | \$ 32   | \$ 12,725                        |
| Other comprehensive income                    |                         |                      |                                  |                         | 1   | 1                                |
| Stock-based compensation expense              |                         |                      | 3                                |                         |   | 3                                |
| Net loss                                      |                         |                      |                                  | (31)                    |   | (31)                             |
| <b>Balance March 31, 2019<br/>(unaudited)</b> | <b><u>3,395,521</u></b> | <b><u>\$ 339</u></b> | <b><u>\$ 2,022</u></b>           | <b><u>\$ 10,304</u></b> | <b><u>\$ 33</u></b>                             | <b><u>\$ 12,698</u></b>          |

See accompanying notes to unaudited condensed financial statements

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

|  | <b>Three Months Ended<br/>March 31,</b> |                      |
|--|---|----------------------|
|  | <b>2020</b>                             | <b>2019</b>          |
| <b>Cash flows from (used in) operating activities</b>                              |   |                      |
| <b>Net loss</b>  | <b>\$ (91)</b>                          | <b>\$ (31)</b>       |
| Adjustments to reconcile net loss to net cash from (used in) operating activities: |   |                      |
| Depreciation and amortization  | 90                                      | 77                   |
| Deferred income taxes  | (4)                                     | 3                    |
| Stock-based compensation expense   | 3                                       | 3                    |
| Interest accrued on treasury bills   | 0                                       | (44)                 |
| Loss on investments  | 3                                       | 0                    |
| Change in:   |   |                      |
| Trade receivables  | 102                                     | (179)                |
| Inventories  | (26)                                    | (20)                 |
| Other current assets   | (45)                                    | (12)                 |
| Accounts payable   | 69                                      | 91                   |
| Accrued expenses   | (20)                                    | 12                   |
| Income tax receivable/payable  | (15)                                    | (12)                 |
| <b>Net cash from (used in) operating activities</b>                                | <b>66</b>                               | <b>(112)</b>         |
| <b>Cash flows from (used in) investing activities</b>                              |   |                      |
| Purchases of treasury bills  | (999)                                   | (3,945)              |
| Proceeds from the maturity of treasury bills                                       | 0                                       | 4,000                |
| Purchase of property and equipment   | 0                                       | (45)                 |
| <b>Net cash from (used in) investing activities</b>                                | <b>(999)</b>                            | <b>10</b>            |
| <b>Cash flows used in financing activities</b>                                     |   |                      |
| Payments on financing lease  | (2)                                     | (1)                  |
| <b>Net cash used in financing activities</b>                                       | <b>(2)</b>                              | <b>(1)</b>           |
| <b>Net decrease in cash and cash equivalents</b>                                   | <b>(935)</b>                            | <b>(103)</b>         |
| Cash and cash equivalents, beginning   | 8,785                                   | 1,057                |
| Cash and cash equivalents, ending  | <u><u>\$ 7,850</u></u>                  | <u><u>\$ 954</u></u> |
| <b>Supplemental cash flow information</b>  |   |                      |
| Cash paid for income taxes   | <u><u>\$ 0</u></u>                      | <u><u>\$ 0</u></u>   |

See accompanying notes to unaudited condensed financial statements

**ELECTRO-SENSORS, INC.**  
**NOTES TO CONDENSED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MARCH 31, 2020**  
**(in thousands except share and per share amounts)**  
(unaudited)

**Note 1. Basis of Presentation**

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions and regulations of the Securities and Exchange Commission to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

This report should be read together with the Company's Annual Report on Form 10-K for the year ended December 31, 2019, including the audited financial statements and footnotes therein.

Management believes that the unaudited financial statements include all adjustments, consisting of normal recurring accruals, necessary to fairly state the financial position and results of operations as of March 31, 2020 and for the three-month periods ended March 31, 2020 and 2019, in accordance with accounting principles generally accepted in the United States of America. The results of interim periods may not be indicative of results to be expected for the year.

**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 every market served. The Company sells these products through an internal sales staff, manufacturers' 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.

**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.

**Fair Value Measurements**

The carrying value of trade receivables, accounts payable, and other financial working capital items approximates fair value at March 31, 2020 and December 31, 2019, due to the short maturity nature of these instruments.



**ELECTRO-SENSORS, INC.**  
**NOTES TO CONDENSED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MARCH 31, 2020**  
**(in thousands except share and per share amounts)**  
(unaudited)

**Intangibles**

Intangible assets are comprised of the HazardPRO technology and a technology license. The Company amortizes the cost of these intangible assets on a straight-line method over their estimated useful lives.

**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") option pricing 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 interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for the estimated life of the option.

As of March 31, 2020, there was approximately \$12 of unrecognized compensation expense related to unvested stock options. The Company expects to recognize this expense over the next three years.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Significant estimates, including the underlying assumptions, consist of 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 COVID-19 pandemic 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.

**Net Loss per Common Share**

Basic and diluted net loss per common share is determined by dividing net loss attributable to common stockholders by the weighted-average common shares outstanding during the period. For the three-month periods ended March 31, 2020 and 2019, 332,500 weighted average common shares for underlying stock options have been excluded from the calculation because their effect would be anti-dilutive. Therefore, the weighted-average shares outstanding used to calculate both basic and diluted loss per common shares are the same.

**ELECTRO-SENSORS, INC.**  
**NOTES TO CONDENSED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MARCH 31, 2020**  
(in thousands except share and per share amounts)  
(unaudited)

**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 A-1+, P-1, and F1+. The Treasury Bills have remaining terms ranging from one month to ten months at March 31, 2020.

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.

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

|   | <u>Cost</u>     | <u>Gross<br/>unrealized<br/>gain</u> | <u>Gross<br/>unrealized<br/>loss</u> | <u>Fair<br/>value</u> |
|---|-----------------|--------------------------------------|--------------------------------------|-----------------------|
| <b>March 31, 2020</b>                       |                 |                                      |                                      |                       |
| Commercial Paper                            | \$ 763          | \$ 0                                 | \$ 0                                 | \$ 763                |
| Treasury Bills                              | 7,749           | 0                                    | 0                                    | 7,749                 |
| Equity Securities                           | 45              | 0                                    | (3)                                  | 42                    |
|   | <u>8,557</u>    | <u>0</u>                             | <u>(3)</u>                           | <u>8,554</u>          |
| Less Cash Equivalents                       | 7,513           | 0                                    | 0                                    | 7,513                 |
| <b>Total Investments, March 31, 2020</b>    | <u>\$ 1,044</u> | <u>\$ 0</u>                          | <u>\$ (3)</u>                        | <u>\$ 1,041</u>       |
| <b>December 31, 2019</b>                    |                 |                                      |                                      |                       |
| Commercial Paper                            | \$ 797          | \$ 0                                 | \$ 0                                 | \$ 797                |
| Treasury Bills                              | 7,734           | 0                                    | 0                                    | 7,734                 |
| Equity Securities                           | 45              | 0                                    | 0                                    | 45                    |
|   | <u>8,576</u>    | <u>0</u>                             | <u>0</u>                             | <u>8,576</u>          |
| Less Cash Equivalents                       | 8,531           | 0                                    | 0                                    | 8,531                 |
| <b>Total Investments, December 31, 2019</b> | <u>\$ 45</u>    | <u>\$ 0</u>                          | <u>\$ 0</u>                          | <u>\$ 45</u>          |

**ELECTRO-SENSORS, INC.**  
**NOTES TO CONDENSED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MARCH 31, 2020**  
(in thousands except share and per share amounts)  
(unaudited)

**Note 3. Fair Value Measurements**

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

**March 31, 2020**

|                   | Carrying amount         |                   | Fair Value Measurement Using |                |                |
|-------------------|-------------------------|-------------------|------------------------------|----------------|----------------|
|                   | <u>in balance sheet</u> | <u>Fair Value</u> | <u>Level 1</u>               | <u>Level 2</u> | <u>Level 3</u> |
| <b>Assets:</b>    |                         |                   |                              |                |                |
| Cash equivalents  |                         |                   |                              |                |                |
| Commercial paper  | \$ 763                  | \$ 763            | \$ 763                       | \$ 0           | \$ 0           |
| Treasury bills    | 6,750                   | 6,750             | 6,750                        | 0              | 0              |
| Treasury bills    | 999                     | 999               | 999                          | 0              | 0              |
| Equity Securities | 42                      | 42                | 0                            | 0              | 42             |

**December 31, 2019**

|                   | Carrying amount         |                   | Fair Value Measurement Using |                |                |
|-------------------|-------------------------|-------------------|------------------------------|----------------|----------------|
|                   | <u>in balance sheet</u> | <u>Fair Value</u> | <u>Level 1</u>               | <u>Level 2</u> | <u>Level 3</u> |
| <b>Assets:</b>    |                         |                   |                              |                |                |
| 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             |

The fair value of the commercial paper and treasury bills is based on quoted market prices in an active market. There is no public market for the available-for-sale equity security owned by the Company. The Company has determined the fair value for this equity security based on financial and other factors that are considered level 3 inputs in the fair value hierarchy.

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

|                      | <u>Three Months Ended March 31,</u> |              |
|----------------------|-------------------------------------|--------------|
|                      | <u>2020</u>                         | <u>2019</u>  |
| Beginning Balance    | \$ 45                               | \$ 45        |
| Change in Fair Value | (3)                                 | 0            |
| Ending Balance       | <u>\$ 42</u>                        | <u>\$ 45</u> |

**ELECTRO-SENSORS, INC.**  
**NOTES TO CONDENSED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MARCH 31 2020**  
**(in thousands except share and per share amounts)**  
(unaudited)

**Note 4. Subsequent Events**

On May 5, 2020, the Company recieved a \$645 loan from the U.S. Small Business Administration through the Paycheck Protection Program (PPP). All or a portion of the loan is forgivable if the Company meets specified requirements regarding the use of these funds over the eight weeks following receipt of loan proceeds. The unforgiven portion of the loan, if any, is payable over eighteen months, after the conclusion of a six month deferral period, and the Company is permitted to repay at any time without penalty. The PPP loan is unsecured and is evidenced by a note in favor of US Bank National Association. See Part II, Item 5, Other Information, in the Form 10-Q.

## **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

### **FORWARD-LOOKING STATEMENTS**

This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding our expectations, beliefs, intentions or strategies regarding the future. Forward-looking statements include, but are not limited to, statements relating to our marketing efforts; our efforts to accelerate future growth or income; our business development activities; our efforts to maintain or reduce production costs; our expected use of cash on hand; our cash requirements; and the sufficiency of our cash flows. Any statement that is not based solely upon historical facts, including our strategies for the future and the outcome of events that have not yet occurred, is a forward-looking statement.

All forward-looking statements in this document are based on information available to us as of the date of this Form 10-Q, and we assume no obligation to update any of these forward-looking statements, other than as required by law. Our actual results could differ materially from those projected or indicated in these forward-looking statements. These forward-looking statements are subject to certain risks and uncertainties that could cause future results to differ materially from our recent results or those projected in the forward-looking statements, including the accuracy of management’s assumptions with respect to industry trends, fluctuations in industry conditions, the accuracy of management’s assumptions regarding expenses and our cash needs and those listed under the heading “Cautionary Statements” under “Item 1—Business,” in our Annual Report on Form 10-K for the year ended December 31, 2019.

### **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. These decisions include the selection of applicable accounting principles and the use of judgment in their application and affect reported amounts and disclosures. Changes in economic conditions or other business circumstances may affect the outcomes of management’s estimates and assumptions. An in-depth description of our accounting estimates can be found in the interim financial statements included in this report and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019. We have not developed new estimates subsequent to those discussed in our Annual Report.

## SELECTED FINANCIAL INFORMATION

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

|                                 | Three Months Ended March 31, |         |
|---------------------------------|------------------------------|---------|
|                                 | 2020                         | 2019    |
| Net sales                       | 100.0 %                      | 100.0 % |
| Cost of goods sold              | 48.0                         | 46.9    |
| Gross profit                    | 52.0                         | 53.1    |
| Operating expenses              |                              |         |
| Selling and marketing           | 23.8                         | 24.1    |
| General and administrative      | 24.2                         | 23.5    |
| Research and development        | 11.3                         | 9.8     |
| Total operating expenses        | 59.3                         | 57.4    |
| Operating loss                  | (7.3)                        | (4.3)   |
| Non-operating income (expense)  |                              |         |
| Loss on investment              | (0.2)                        | 0.0     |
| Interest income                 | 1.7                          | 2.2     |
| Other income                    | 0.1                          | 0.1     |
| Total non-operating income, net | 1.6                          | 2.3     |
| Loss before income tax benefit  | (5.7)                        | (2.0)   |
| Benefit from income taxes       | (1.0)                        | (0.4)   |
| Net loss                        | (4.7) %                      | (1.6) % |

The following paragraphs discuss the Company's performance for the three months ended March 31, 2020 and 2019.

## RESULTS OF OPERATIONS (in thousands)

### Net Sales

Net sales for the three-month period ended March 31, 2020 were \$1,923, a decrease of \$85, or 4.2%, from \$2,008 during the comparable period in 2019. As the quarter progressed, sales became less predictable as many of our customers were increasingly impacted by the COVID-19 pandemic. During March 2020, several of our customers identified Electro-Sensors as an essential supplier, in part due to the use of our products in the agricultural production segment of the American economy, requiring us to remain fully operational to continue to supply critical infrastructure industries.

### Gross Profit

Gross profit for the first quarter of 2020 decreased \$68, or 6.4%, over the same period in 2019. Gross margin decreased in the first quarter of 2020 to 52.0% from 53.1% during the same period in 2019. The decrease in the gross margin percentage was primarily due to a change in product mix and higher material costs resulting from the increase in government tariff charges that started during the second half of 2019.

### **Operating Expenses**

Total operating expenses decreased \$13, or 1.1%, for the first quarter of 2020 compared to the same period in 2019 and increased as a percentage of net sales to 59.2% from 57.4%.

- Selling and marketing expenses in the first quarter of 2020 decreased \$27, or 5.6%, from the same period in 2019 and decreased as a percentage of net sales to 23.8% from 24.1%. The decrease resulted primarily from lower outside sales representative compensation due to changes in commission plans and a decrease in trade show related expenses due to cancelled or rescheduled shows.
- General and administrative expenses decreased \$7, or 1.5%, for the first quarter of 2020 compared to the same period in 2019, but increased as a percentage of net sales to 24.2% from 23.5%. The decrease was due primarily to decreased expenses related to computer supplies, software, and training, partially offset by an increase in legal fees related to corporate governance.
- Research and development expenses increased \$21, or 10.7%, in the first quarter of 2020 from the same period in 2019 and increased as a percentage of net sales to 11.3% from 9.8%. The increase was due to higher lab testing costs to obtain third party certifications.

### **Non-Operating Income (Net)**

Net non-operating income decreased by \$15, or 32.6%, for the first quarter of 2020 compared to the same period in 2019, primarily a result of decreased interest income earned as a result of lower interest rates on Treasury Bills.

### **Loss Before Income Tax Benefit**

Loss before income tax benefit was \$110 for the first quarter of 2020, representing an increase of \$70, or 175.0%, compared to a loss before income tax benefit of \$40 for the same period in 2019. The increase was primarily the result of lower net sales discussed above.

### **Income Tax Benefit**

The Company's income tax benefit increased to \$19, or 1.0% of net sales, in the first quarter of 2020 compared to a benefit of \$9, or 0.4% of net sales, in the first quarter of 2019.

## **LIQUIDITY AND CAPITAL RESOURCES**

Cash and cash equivalents were \$7,850 at March 31, 2020 and \$8,785 at December 31, 2019. The decrease was primarily the result of cash used to purchase treasury bills. One of the treasury bills purchased during the first quarter of 2020 was considered an available-for-sale security.

Cash generated from operating activities was \$66 for the three months ended March 31, 2020 as compared to cash used in operating activities of \$112 for the three months ended March 31, 2019. The \$178 increase in cash from operations was due to a decrease in trade receivables partially offset by an increase in other current assets and a decrease in accrued expenses. The decrease in trade receivables was due to decreased net sales and the timing of collections on accounts. The increase in other current assets was due to increased deposits for computers, trade shows, and travel. The decrease in accrued expenses was due to changes in accrued compensation due to modifications of outside and inside commission plans.

Cash used in investing activities was \$999 for the three months ended March 31, 2020 as compared to cash generated from investing activities of \$10 for the three months ended March 31, 2019. During the three months ended March 31, 2020 the Company had net purchases of treasury bills of \$999 compared to net proceeds from maturities of treasury bills of \$55 during the three months ended March 31, 2019. In addition, the Company purchased \$45 of property, equipment, and intangibles during the three months ended March 31, 2019.

Cash used in financing activities in the three months ended March 31, 2020 and 2019 was \$2 and \$1, respectively. The cash used in both periods was for principal payments on a financing lease on right-to-use assets.

Subject to the following section, the Company believe its ongoing cash requirements will be primarily for capital expenditures, research and development, working capital, and growth initiatives. Management believes that our cash on hand and any cash generated from operations will be sufficient to meet our cash requirements through at least the next 12 months.

### **COVID-19 Pandemic and PPP Loan**

During the quarter ended March 31, 2020, the Company's net sales and gross profit decreased, which caused its net loss to increase. The Company also experienced a softening in sales prospects late in the first quarter and net sales remain unpredictable into the second quarter. Due to the ongoing uncertainty about the severity and duration associated with the COVID-19 pandemic, the Company considered furloughing or eliminating employees and taking other measures to reduce operating costs until there is more certainty about the short-term and long-term effects of the COVID-19 pandemic on the nation's economy and the Company's business.

On May 5, 2020, the Company received \$645 in support from the U.S. federal government in the form of a Paycheck Protection Program Loan ("PPP Loan") established as part of the Coronavirus Aid, Relief, and Economic Security Act. The PPP Loan is unsecured and is evidenced by a note in favor of US Bank National Association. See Part II, Item 5, Other Information, of this Form 10-Q.



## **COVID-19 Pandemic Discussion**

As a result of the COVID-19 pandemic, we experienced a weaker than anticipated first quarter of 2020 and we expect these results may continue. We currently expect our second quarter financial results will be negatively impacted, potentially to a material degree. Reductions in net sales have not been offset by a proportional decrease in expense, as we continue to incur cost such as compensation, administrative expenses, and depreciation and amortization, resulting in a negative effect on the relationship between our costs and net sales. The impact may be partially offset by the application of PPP loan forgiveness. However, at this time we are unable to determine the effect of the offset as final guidance has not yet been published regarding the PPP loan forgiveness and related tax impacts.

We believe the pandemic will slow larger orders as customers delay projects in order to conserve cash, which will slow the demand for our products.

We, typically, have multiple sources for components. However, we are starting to experience extended delivery times as vendors have difficulty either sourcing components or were closed for a period of time.

As of the date of this filing, we expect our business will continue to be negatively impacted, but cannot currently determine the significance and duration of the pandemic on our business.

### ***Future Business Development Activities***

The Company continues to seek growth opportunities, both internally through the Company's existing portfolio of products, technologies and markets, as well as externally through technology partnerships or related-product acquisitions.

### ***Off-balance Sheet Arrangements***

As of March 31, 2020, the Company had no off-balance sheet arrangements or transactions.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Not Applicable.

### **Item 4. Controls and Procedures**

#### ***Evaluation of Disclosure Controls and Procedures***

Based on an evaluation with the participation of the Company's management, the Company's principal executive officer and principal financial officer has concluded that the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act"), were effective as of March 31, 2020.

#### ***Changes in Internal Control Over Financial Reporting***

There were no changes in the Company's internal control over financial reporting during the first quarter of 2020 that 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.

## **PART II – OTHER INFORMATION**

### **Item 1. Legal Proceedings – None**

### **Item 1A. Risk Factors – Not Applicable**

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds – None**

### **Item 3. Defaults Upon Senior Securities – None**

### **Item 4. Mine Safety Disclosures – Not Applicable**

### **Item 5. Other Information**

#### **Paycheck Protection Plan Loan ("PPP Loan")**

On May 5, 2020, the Company received \$645,180 in support (the "PPL Loan") from the U.S. federal government in the form of a Paycheck Protection Program loan established as part of the Coronavirus Aid, Relief, and Economic Security Act. The PPP Loan is unsecured and is evidenced by a note in favor of US Bank National Association as the lender (the "Note"), which is filed as Exhibit 10.1 to this Form 10-Q and incorporated by reference herein

The interest rate on the Note is 1.0% per annum. Payments of principal and interest are deferred for 180 days from the date of the Note (the deferral period). The Paycheck Protection Program provides a mechanism for forgiveness of up to the full amount borrowed as long as the Company uses the loan proceeds during the eight-week period after the loan origination for eligible purposes, including U.S. payroll costs, certain benefits costs, rent and utilities costs, and maintains its employment and compensation levels, subject to certain other requirements and limitations. The amount of loan forgiveness is subject to reduction, among other reasons, if the Company terminates employees or reduces salaries or wages during the eight-week period. Any unforgiven portion of the PPP Loan is payable over a two-year term, with payments deferred during the deferral period. The Company is permitted to prepay the Note at any time without payment of any premium. The Note contains customary events of default, including, among others, those relating to failure to make a payment, bankruptcy, material defaults on other indebtedness, breaches of representations, and material adverse changes.

### **Item 6. Exhibits**

| <b>Exhibit</b> | <b>Description</b>   |
|----------------|--|
| 10.1           | Electro-Sensors, Inc. Small Business Administration Payroll Protection Program Loan Agreement for \$645,180 dated as of May 5, 2020  |
| 31.1           | Certification of CEO and CFO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 32.1           | Certification of CEO and CFO Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  |
| 101            | The following financial information from Electro-Sensors, Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2020, formatted in iXBRL (Inline Extensible Business Reporting Language), (i) Condensed Balance Sheets as of March 31, 2020 and December 31, 2019, (ii) Condensed Statements of Comprehensive Loss for the three months ended March 31, 2020 and March 31, 2019 (iii) Condensed Statements of Changes in Stockholders' Equity for the three months ended March 31, 2020 and March 31, 2019, (iv) Condensed Statements of Cash Flows for the three months ended March 31, 2020 and March 31, 2019, and (v) Notes to Financial Statements. |

## **SIGNATURES**

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

**Electro-Sensors, Inc.**

May 11, 2020

/s/ David L. Klenk

David L. Klenk  
Chief Executive Officer and Chief Financial Officer  
(Principal Executive Officer and Principal Financial  
Officer)

# U.S. BANK® SBA PAYROLL PROTECTION LOAN

## U.S. Bank® SBA Payroll Protection Loan

Note Date: 05/05/2020

Tax ID Number: 41-0943459

Loan Amount: \$645,180.00

## Borrower

Electro-Sensors, Inc.

Minnetonka, MN 55343

Type of Organization: C-Corp

State of Registration: MN-Minnesota

1. **Loan ("Loan").** FOR VALUE RECEIVED, the undersigned borrower ("**Borrower**") promises to pay to the order of U.S. Bank National Association (the "**Bank**"), the principal sum of \$645,180.00 (the "**Loan Amount**"), in accordance with the terms of this U.S. Bank® SBA Payroll Protection Loan (this "**Agreement**").

- 1.1 **SBA Guaranty.** In response to the Covid-19 pandemic the U.S. Congress has passed the CARES Act ("**Act**") which among other things, includes amending Section 7(a) of the Small Business Act (15 U.S.C. 636(a)) to provide for this short-term SBA lending program between February 15, 2020 to June 30, 2020 (the "**Covered Period**") for payroll protection of small businesses, nonprofit organizations, veterans organizations, or tribal business entities (the "**Program**"). The Loan evidenced by this Agreement is guaranteed by the U.S. Small Business Administration ("**SBA**"), information regarding which can be obtained from the SBA directly or at its website: [www.sba.gov](http://www.sba.gov). Under this Program, if the proceeds of this Loan were used by the Borrower for eligible expenses as defined in Section 1102 of the Act to include payroll costs, continuation of health care benefits, employee salaries, mortgage interest, rent, utilities, balances on SBA Economic Injury Disaster Loans ("**EIDL**") and interest on other outstanding debt incurred prior to February 15, 2020 ("**Eligible Expenses**"), then Borrower may apply for loan forgiveness of all Eligible Expenses excluding interest on outstanding non-mortgage debt, and existing EIDL balances not used for forgivable purposes ("**Forgivable Expenses**") from the SBA as outlined below. Upon Borrower certification of the amount of Loan proceeds used to pay Forgivable Expenses, such expenses will be forgiven as a principal payment on the Borrower's Loan. The remaining Loan balance, if any, will be re-amortized and paid by the Borrower as detailed further in this Agreement. It is a condition of making this Loan that the SBA accept the Loan. In no event shall the interest rate, fees or other charges under this Agreement exceed the maximum rate or amounts permitted for the SBA Loan Program or any other maximum rates of interest imposed by applicable law. This Loan is only available to Borrowers that have their principal place of business in the United States. To the extent feasible, Borrower agrees to purchase only American-made equipment and products with the proceeds of this Loan. The SBA Guaranty does not affect the liability of the Borrower under this Agreement.

- 1.2 **Forgiveness.** Within 60 days from the Note Date, the Borrowers may request all or part of their Loan be forgiven by submitting an application for forgiveness and documentation verifying the number of fulltime equivalent employees on payroll and their pay rates during the eight weeks after this Note Date. Such documentation shall include payroll tax filings with the Internal Revenue Service, state income, state payroll, and state unemployment insurance filings, cancelled checks, payment receipts, transcripts of accounts, or other documents verifying payments for Forgivable Expenses ("Forgiveness Documentation"). Seventy-five percent of Eligible Expenses must be used for payroll related expenses and up to twenty-five percent may be used for other Eligible Expenses, to qualify for forgiveness. Borrower must also provide the Bank with a certification that the Forgiveness Documentation is true and correct, and the amount of requested forgiveness was used for Forgivable Expenses. After approval of the forgiveness amount and 6 month deferral, the Bank will provide the Borrower written notification of the remaining balance and re-amortization of the Loan, if any. Forgiveness cannot be provided without the Borrower's submission to the Bank of all the documents required by this Section 1.2.

- 1.3 **Interest.** The unpaid principal balance will bear interest at an annual rate of 1.00%.

**1.4 Payment Schedule.** Principal and interest are payable in 18 installments of \$36,051.07 each, beginning on 2020-12-05 and on the same date of each consecutive month thereafter (except that if a given month does not have such a date, the last day of such month), plus a final payment equal to all unpaid principal and accrued interest on 2022-05-05, the maturity date. Installment payment amounts will be re-amortized after the Deferral Period and partial loan forgiveness credit is applied, at such time an updated Payment Schedule will be provided to Borrower. There is no penalty for Borrowers who pay off their Loan early.

**1.5 Automatic Payments.** If this box is checked, then at all times that this Agreement is in effect, Borrower hereby authorizes the Bank to automatically deduct the amount of all payments required under this Agreement from:

Borrower's business deposit account number held with the Bank.

Borrower's business deposit account held at (Financial Institution) with Account Number and Routing Number.

This account is the "**Payment Source Account.**" If there are insufficient funds in the Payment Source Account to pay the required payment, Borrower agrees to pay all fees on the Payment Source Account, which result from the automatic deductions, including any overdraft/NSF charges and any returned payment fee. If for any reason the Bank does not charge the Payment Source Account for payment, or if an automatic payment from the Payment Source Account is reversed, the payment is still due according to this Agreement. The number of withdrawals from the Payment Source Account may be limited, as set out in the customer agreement for that account. The Bank may cancel the automatic payment deduction from the Payment Source Account at any time in its discretion.

**1.6 Calculation of Interest and Maximum Rate.** Interest will be computed for the actual number of days principal is unpaid, using a daily factor obtained by dividing the stated interest rate by 360. In no event will the interest rate hereunder exceed that permitted by applicable law. If any interest or other charge is finally determined by a court of competent jurisdiction to exceed the maximum amount permitted by law, the interest or charge shall be reduced to the maximum permitted by law, and the Bank may credit any excess amount previously collected against the balance due or refund the amount to Borrower.

**1.7 Late Payment Fee.** Subject to applicable law, if any payment is not made on or before its due date, the Bank may collect a delinquency charge of \$15.00 or 5% of the delinquent amount, whichever is less; provided, however, that if any portion of the Loan evidenced by this Agreement has been guaranteed by the U.S. Small Business Administration, the late fee shall not exceed 5% of the delinquent amount. Collection of the late payment fee shall not be deemed to be a waiver of the Bank's right to declare a default hereunder.

**1.8 Loan Purpose.** Borrower represents that the proceeds of the Loan evidenced by this Agreement will be used for business purposes. Borrower specifically represents and warrants the following business purpose uses of the Loan proceeds; The funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments, and utility payments.

**1.9 Deposits and Paying Procedure.** The Bank is authorized and directed to credit any of Borrower's accounts with the Bank (or to the account Borrower designates in writing) for all Loans made hereunder, and the Bank is authorized to debit such account or any other account of Borrower with the Bank for the amount of any principal, interest or expenses due under this Agreement or other amount due hereunder on the due date with respect thereto. Payments due under this Agreement and other Loan Documents will be made in lawful money of the United States. All payments may be applied by the Bank to principal, interest and other amounts due under the Loan documents in any order, which the Bank elects. If, upon any request by Borrower to the Bank to issue a wire transfer, there is an inconsistency between the name of the recipient of the wire and its identification number as specified by Borrower, the Bank may, without liability, transmit the payment via wire based solely upon the identification number.

**1.10 Returned Payment Charge.** For each payment made by Borrower to the Bank that is returned or rejected (such as a check that is returned unpaid, or an automated transfer that is rejected), Borrower shall pay the Bank a returned payment fee of \$25.00.

2. **Warranties/Covenants.** Borrower continuously warrants and agrees as follows:
- 2.1 **Borrower's Name, Location; Notice of Location Changes.** Unless otherwise disclosed to the Bank in writing prior to the execution of this Agreement, Borrower's name and organizational structure has remained the same during the past five years. The Borrower will continue to use only the name set forth with Borrower's signature unless Borrower gives the Bank prior written notice of any change. Furthermore, Borrower shall not do business under another name nor use any trade name without giving 10 days prior written notice to the Bank. The Borrower will not change its status or organizational structure without the prior written consent of the Bank. The address appearing at the top of this Agreement is Borrower's chief executive office (or residence if Borrower is a sole proprietor).
  - 2.2 **Financial Information.** The Borrower will (i) maintain accounting records in accordance with generally recognized and accepted principles of accounting consistently applied throughout the accounting periods involved; (ii) provide the Bank with such information concerning its business affairs and financial condition (including insurance coverage) as the Bank may reasonably request.
  - 2.3 **Setoff.** The Borrower grants to the Bank an express contractual right to set off against all depository account balances, cash and any other property of Borrower now or hereafter in the possession of the Bank and the right to refuse to allow withdrawals from any account (collectively "Setoff"). The Bank may, at any time upon the occurrence of a default hereunder (notwithstanding any notice requirements or grace/cure periods under this or other agreements between Borrower and the Bank) Setoff against the Obligations whether or not the Obligations (including future installments) are then due or have been accelerated, all without any advance or contemporaneous notice or demand of any kind to Borrower, such notice and demand being expressly waived.
  - 2.4 **Borrower Compliance.** The Borrower represents and warrants they will comply with all rules, laws, and obligations set forth under the SBA Paycheck Protection Program.
  - 2.5 **Prohibition of Executive Officer Status.** Borrower is not an Executive Officer of Bank as defined under 12 C.F.R. §215.2, if Borrower should become an Executive Officer of Bank, Borrower understands Bank reserves the right to require Borrower to repay on demand, any amount outstanding on the loan made under this Agreement.
3. **Default.** Notwithstanding any cure periods described below, Borrower shall immediately notify the Bank in writing when Borrower obtains knowledge of the occurrence of any event of default specified below. Regardless of whether Borrower has given the required notice, the occurrence of one or more of the following shall constitute a default:
- 3.1 **Nonpayment.** The Borrower shall fail to pay (i) any interest due or any fees, charges, costs or expenses under this Agreement by five (5) days after the same becomes due; or (ii) any principal amount of this Agreement when due.
  - 3.2 **Nonperformance.** The Borrower shall fail to perform or observe any agreement, term, provision, condition, or covenant (other than a default occurring under this paragraph 3) required to be performed or observed by Borrower hereunder or under any other agreement with or in favor of the Bank.
  - 3.3 **Misrepresentation.** Any financial information, statement, certificate, representation or warranty given to the Bank by Borrower (or any of their representatives) in connection with entering into this Loan and/or borrowing hereunder, or required to be furnished under the terms hereof, shall prove untrue or misleading in any material respect (as determined by the Bank in the exercise of its judgment) as of the time when given.
  - 3.4 **Default on Other Obligations.** The Borrower is in default under the terms of any loan agreement, promissory note, lease, conditional sale contract or other agreements, document or instrument evidencing, governing or severing any indebtedness owing by Borrower to the Bank or any indebtedness in excess of \$10,000 owing by Borrower to any third party, and the period of grace, if any, to cure said default shall have passed.
  - 3.5 **Judgments.** Any judgment shall be obtained against Borrower, which, together with all other outstanding unsatisfied judgments against Borrower, shall exceed the sum of \$10,000 and shall remain unvacated, unbonded or unstayed for a period of thirty (30) days following the date of entry thereof.

**3.6 Inability to Perform; Bankruptcy/Insolvency.** (i) The Borrower shall die or cease to exist, or (ii) any bankruptcy, insolvency or receivership proceedings, or an assignment for the benefit of creditors, shall be commenced under any federal or state law by or against Borrower; or (iii) Borrower shall become the subject of any out-of-court settlement with its creditors; or (v) Borrower is unable or admits in writing its inability to pay its debts as they mature.

**3.7 Adverse Change; Insecurity.** (i) There is a material adverse change in the Borrower's business, properties, financial condition or affairs.

**4. Acceleration of Obligations.** Upon the occurrence of any of the events identified in paragraph 3 and the passage of any applicable cure periods, the Bank may at any time thereafter, by written notice to Borrower, declare the unpaid principal balance of any Obligations, together with the interest accrued thereon and other amounts accrued hereunder, to be immediately due and payable; and the unpaid balance shall thereupon be due and payable, all without presentation, demand, protest or further notice of any kind, all of which are hereby waived, and notwithstanding anything to the contrary contained herein. Upon the occurrence of any event under paragraph 3.6, the unpaid principal balance of any Obligations, together with all interest accrued thereon and other amounts accrued hereunder, shall thereupon be immediately due and payable, all without presentation, demand, protest or notice of any kind, all of which are hereby waived, and notwithstanding anything to the contrary contained herein.

**5. Cumulative Remedies; Notice; Waiver.** The Bank may enforce its rights and remedies under this Agreement upon default. In addition to the remedies for default set forth in this Agreement, the Bank upon default shall have all other rights and remedies for default provided by the Uniform Commercial Code, as well as any other applicable law and this Agreement. The rights and remedies specified herein are cumulative and are not exclusive of any rights or remedies, which the Bank would otherwise have.

**5.1 Waiver by the Bank.** The Bank may permit Borrower to attempt to remedy any default without waiving its rights and remedies hereunder, and the Bank may waive any default without waiving any other subsequent or prior default by Borrower. Furthermore, delay on the part of the Bank in exercising any right, power or privilege hereunder or at law shall not operate as a waiver thereof; nor shall any single or partial exercise of such right, power or privilege preclude other exercise thereof or the exercise of any other right, power or privilege. No waiver or suspension shall be deemed to have occurred unless the Bank has expressly agreed in writing specifying such waiver or suspension.

**6. Waivers; Relationship to Other Documents.** All Borrowers waive presentment, protest, demand, and notice of dishonor. The warranties, covenants and other obligations of Borrower (and the rights and remedies of the Bank) in this Agreement and all related documents are intended to be cumulative and to supplement each other.

**7. Expenses and Attorneys' Fees.** The Borrower will reimburse the Bank and any participant in the Obligations ("Participant") for all attorneys' fees and all other costs, fees and out-of-pocket disbursements incurred by the Bank or any Participant in connection with the preparation, execution, delivery, administration, defense and enforcement of this Agreement, including fees and costs related to any waivers or amendments with respect thereto. The Borrower will also reimburse the Bank and any Participant for all costs of collection before and after judgment, and the costs of preservation and/or liquidation of any collateral.



8. **Applicable Law; Interpretation; Joint Liability.** This Agreement shall be governed by and interpreted in accordance with the internal laws of the state of Ohio, except to the extent superseded by Federal law. THE BORROWER HEREBY CONSENTS TO THE EXCLUSIVE JURISDICTION OF ANY STATE OR FEDERAL COURT SITUATED IN THE COUNTY OR FEDERAL JURISDICTION OF THE BANK'S BRANCH WHERE THE LOAN WAS ORIGINATED, AND WAIVES ANY OBJECTION BASED ON FORUM NON CONVENIENS, WITH REGARD TO ANY ACTIONS, CLAIMS, DISPUTES OR PROCEEDINGS RELATING TO THIS NOTE, THE COLLATERAL, ANY OTHER LOAN DOCUMENT, OR ANY TRANSACTIONS ARISING THEREFROM, OR ENFORCEMENT AND/OR INTERPRETATION OF ANY OF THE FOREGOING. Invalidity of any provisions of this Agreement shall not affect any other provision. Nothing herein shall affect the Bank's rights to serve process in any manner permitted by law or limit the Bank's right to bring proceedings against Borrower in the competent courts of any other jurisdiction or jurisdictions. This Agreement, and any amendment hereto (regardless of when executed) will be deemed effective and accepted only upon the Bank's receipt of the executed originals thereof. If there is more than one Borrower, the liability of Borrowers shall be joint and several, and the reference to "Borrower" shall be deemed to refer to all Borrowers. When SBA is the holder, this Note will be interpreted and enforced under Federal law, including SBA regulations. The Bank or SBA may use state or local procedures for filing papers, giving notice, and other purposes. By using such procedures, SBA does not waive any federal immunity from state or local control, penalty, tax, or liability. As to this Loan, Borrower may not claim or assert against SBA any local or state law to deny any obligation, defeat any claim of SBA, or preempt federal law.
9. **Participations/Successors.** The Bank may, at its option, sell all or any interests in this Agreement to other financial institutions (the "Participant"), and in connection with such sales (and thereafter) disclose any financial information the Bank may have concerning Borrower to any such Participant or potential Participant. This provision does not obligate the Bank to supply any information or release Borrower from its obligation to provide such information. The rights, options, powers and remedies granted in this Agreement will extend to the Bank and to its successors and assigns, will be binding upon Borrower and its successors and assigns and will be applicable hereto and to all renewals and/or extensions hereof.
10. **Copies; Entire Agreement; Modification.** The Borrower hereby acknowledges the receipt of a copy of this Agreement. **IMPORTANT: READ BEFORE SIGNING. THE TERMS OF THIS AGREEMENT SHOULD BE READ CAREFULLY BECAUSE ONLY THOSE TERMS IN WRITING AND EXPRESSING CONSIDERATION ARE ENFORCEABLE. NO OTHER TERMS OR ORAL PROMISES NOT CONTAINED IN THIS WRITTEN CONTRACT MAY BE LEGALLY ENFORCED. THE TERMS OF THIS AGREEMENT MAY ONLY BE CHANGED BY ANOTHER WRITTEN AGREEMENT. THIS NOTICE SHALL ALSO BE EFFECTIVE WITH RESPECT TO ALL OTHER CREDIT AGREEMENTS NOW IN EFFECT BETWEEN BORROWER AND THE BANK. A MODIFICATION OF ANY OTHER CREDIT AGREEMENTS NOW IN EFFECT BETWEEN BORROWER AND THE BANK, WHICH OCCURS AFTER RECEIPT BY BORROWER OF THIS NOTICE, MAY BE MADE ONLY BY ANOTHER WRITTEN INSTRUMENT. ORAL OR IMPLIED MODIFICATIONS TO SUCH CREDIT AGREEMENTS ARE NOT ENFORCEABLE AND SHOULD NOT BE RELIED UPON.**
11. **Waiver of Jury Trial.** **TO THE EXTENT PERMITTED BY LAW, BORROWER AND BANK HEREBY JOINTLY AND SEVERALLY WAIVE ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING RELATING TO ANY OF THE LOAN DOCUMENTS, THE OBLIGATIONS THEREUNDER, OR ANY TRANSACTION ARISING THEREFROM OR CONNECTED THERETO. BORROWER AND BANK EACH REPRESENTS TO THE OTHER THAT THIS WAIVER IS KNOWINGLY, WILLINGLY, AND VOLUNTARILY GIVEN.**
12. **Attachments.** All documents attached hereto, including any appendices, schedules, riders, and exhibits to this Loan Note are hereby expressly incorporated by reference.

**SIGNATURES**

By signing this Agreement, each person ("Signer"), individually and on behalf of Borrower, requests the Loan from the Bank. Each Signer is authorized to sign on behalf of Borrower and will provide business resolutions to the Bank upon request. Each Signer has read and agrees to all applicable provisions. Each Signer authorizes the Bank to (1) obtain credit records and other credit and employment information about the Signers personally and the Borrower (now and in the future), including from state and federal tax authorities, for deciding whether to approve the requested Loan and for later periodic account review and collection purposes, and (2) furnish information about the Borrower to credit bureaus, other Signers, and other persons who claim to be authorized by the Borrower to receive such information. The Borrower and each Signer guaranty that all information in this Agreement is correct and agree to notify the Bank if any information changes. All Loan proceeds shall be used only for business purposes generally, and for the specific purposes described in this Agreement.

By:        /s/ David L. Klenk  
Name:     David L. Klenk  
Title:     President

**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-Q 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.

May 11, 2020

/s/ David L. Klenk

David L. Klenk  
Chief Executive Officer and Chief Financial Officer

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

In connection with the Quarterly Report of Electro-Sensors, Inc. (the “Company”) on Form 10-Q for the quarter ended March 31, 2020 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.

May 11, 2020

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/s/ David L. Klenk  
David L. Klenk  
Chief Executive Officer and Chief Financial Officer