
**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, 2021**

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

(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, 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	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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 \$10,100,000 based upon the closing price of its common stock as reported on The Nasdaq Stock Market® on June 30, 2021.

The number of shares outstanding of the registrant's Common Stock, \$0.10 par value, on March 30, 2022 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, 2021

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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.

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 a complete line of monitoring and control systems for a wide range of industrial machine applications. The systems measure machine production and operation rates, as well as 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.

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 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.

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 the user's processes. The simple but powerful interface gives the user insight into the user's internal operations as the user strives to maximize safety and facility runtime, while minimizing costs associated with unscheduled maintenance and unplanned downtime. 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. 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, both nationally and internationally. In 2021, we had international sales through distributors in the following countries; Canada, Mexico, Brazil, Chile, Guatemala, Germany, Peru, United Kingdom, Ukraine, Egypt, Saudi Arabia, United Arab Emirates, South Africa, Tunisia, India, Australia, China, the Republic of Korea, Vietnam, Malaysia, Philippines, Thailand, and Singapore. Sales to customers outside the United States represented approximately 11.6% of 2021 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 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 strategic investments that we believe present good opportunities for the Company and its shareholders.

In addition to enhanced operational safety, 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 sensors and systems from a broad range of industrial and commercial businesses. Among our competitors are 4B Elevator Components Ltd., Maxi-Tronic, Inc., Siemens Industry, Inc., and Ag Growth International Inc. (AGI). 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 challenges include the fact that several of our competitors are larger, may have better established names, have a broader range of sensing instruments, and have larger sales forces and capital resources.

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. In 2021, we experienced increased disruptions in our supply chain, resulting in difficulty sourcing parts. Additionally, we experienced price increases for many of the components used in our products. In some situations, we are modifying product designs to accommodate new components that are more readily available. There is no guarantee that we will continue to be successful in updating these designs and sourcing alternative components and material. We are also experiencing delays in our shipping and transportation services, which may affect our ability to make timely deliveries to our customers. We continue to closely watch lead times and availability of components. We are continually assessing our inventory levels and may take actions as necessary to minimize disruptions to our supply chain such as maintaining larger levels of inventories than we have in the past, but these actions may not be successful if significant disruptions occur.

Customers

We do not depend upon a single or a few customers for a material (10% or more) portion of our sales.

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 or business acquisitions. In addition, we may make strategic or other investments that we believe present good opportunities for the Company and its shareholders, and we substantially increased these business development activities in the second half of 2021.

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 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.

Human Capital

As of December 31, 2021, the Company had 33 employees and two temporary employees, all of whom are full-time and based in the United States. We consider our relations with our employees to be good. None of our employees are currently represented by a labor union.

The Company views its employees and culture as keys to its success. The Company aims to attract and retain qualified personnel and provides wages and benefits that are competitive locally to reward employees for performance. The Company values innovation, inclusion and diversity, safety and engagement as they attract, develop, and retain the best talent.

The health and safety of our employees is our top priority. In response to the COVID-19 pandemic, the Company implemented a workplace safety plan, following CDC guidelines and federal and local mandates, to protect employees and minimize the potential risk of an outbreak within the Company. We believe the Company has generally been successful implementing proactive measures to protect the health and safety of its employees while maintaining business continuity and high levels of service to our customers.

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, supply chain disruptions, downturns in the markets we serve, geopolitical events, and economic disruptions such as weather related events or the effects of the COVID-19 pandemic. 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) our ability to continue to obtain parts and materials for our products from various manufacturers and distributors in a timely manner and at reasonable prices, (iv) the value of our intellectual property, (v) our competitive position in the marketplace, (vi) the effect of governmental regulations on our business, (vii) our employee relations, (viii) the adequacy of our facilities, (ix) our intention to develop new products, (x) the possibility of us acquiring compatible businesses or product lines as part of our growth strategy, (xi) our future cash requirements and use of cash, and (xii) the effect that the continuing COVID-19 pandemic may have on the efficiency of our business operations, our customer base, and the domestic or worldwide economy.

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 obligation 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;
- comply with any new government regulations that may be adopted to require companies to reduce carbon emissions or to disclose their carbon footprint, including the carbon footprint of components to manufacturers;
- 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;
- offset the effect of inflation on component prices and labor by increasing prices on finished products;
- 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 2022.

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 24, 2022, we had 63 shareholders of record who held 872,599 shares of the Company’s common stock. In addition, nominees held an additional 2,522,922 shares for approximately 1,300 shareholders holding shares in street name.

From time to time, we may be required to repurchase our common stock as a result of Employee Stock Ownership Plan (“ESOP”) obligations described in Note 10 to our 2021 financial statements. We did not repurchase any common stock during the years ended December 31, 2021 and 2020.

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,	
	2021	2020
Net sales	100.0%	100.0%
Cost of goods sold	45.7	48.4
Gross profit	54.3	51.6
Operating expenses		
Selling and marketing	16.0	21.2
General and administrative	23.1	22.1
Research and development	10.2	11.0
Total operating expenses	49.3	54.3
Operating income (loss)	5.0	(2.7)
Non-operating income (expense)		
Interest income	0.1	0.5
Other income (expense)	0.2	0.0
Total non-operating income, net	0.3	0.5
Income (loss) before income taxes	5.3	(2.2)
Income tax expense (benefit)	0.6	(0.6)
Net income (loss)	4.7%	(1.6)%

The following paragraphs discuss the Company’s performance for years ended December 31, 2021 and 2020.

Comparison of 2021 vs 2020 (dollars in thousands)

Net Sales

Net sales for 2021 were \$8,607, an increase of \$986, or 12.9%, from \$7,621 in 2020. The increase in sales was driven primarily by increased domestic orders for agricultural and industrial automation applications. International sales during the year were flat as compared to the prior year, with increased sales to Canada primarily offset by decreased sales to China.

Gross Profit

Gross profit for 2021 increased \$747, or 19.0%, to \$4,677 from \$3,930 in 2020. Gross margin in 2021 was 54.3% compared to 51.6% in 2020. The increase in gross margin was primarily due to improved factory and overhead utilization resulting from higher levels of manufacturing to support the increase in net sales.

Operating Expenses

Total operating expenses increased \$102, or 2.5%, to \$4,236 in 2021 from \$4,134 in 2020, but decreased as a percentage of net sales to 49.3% from 54.3%. The increase in operating expense dollars was primarily due to increases in legal and other professional fees and contract engineering for product enhancements.

- Selling and marketing expenses decreased \$239, or 14.8%, to \$1,373 in 2021 from \$1,612 in 2020, and decreased as a percentage of net sales to 16.0% from 21.2%. The decrease was primarily from lower sales headcount, partially offset by an increase in tradeshow related expenses.
- General and administrative expenses increased \$301, or 17.9%, to \$1,987 in 2021 from \$1,686 in 2020, and increased slightly as a percentage of net sales to 23.1% from 22.1%. The higher expenses were primarily due to legal and other professional fees related to the Company's increased corporate and business development activities, partially offset by a decrease in amortization expense related to HazardPRO technology which was fully amortized in the third quarter of 2021.
- Research and development expenses increased \$40, or 4.8%, to \$876 in 2021 compared to \$836 in 2020, but decreased as a percentage of net sales to 10.2% from 11.0%. The increase was primarily due to higher contract engineering costs related to product enhancements.

Operating Income (Loss)

Operating income was \$441 in 2021 compared to an operating loss of \$204 in 2020, an increase of \$645, or 316.2%. The increase to operating income was primarily related to the increase in net sales and gross margin.

Non-Operating Income (Expense)

Non-operating income decreased \$14 to \$18 in 2021 from \$32 in 2020, primarily as a result of less interest income earned as a result of lower interest rates on Treasury Bills, partially offset by an increase in the value of our investment in a non-publicly traded company.

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 expense was \$49 in 2021 compared to an income tax benefit of \$48 in 2020. The increase in the tax expense was due primarily to net income before income taxes in 2021 compared to a net loss before income taxes in 2020. Detailed information on our income tax provision is provided in Note 11 to our financial statements.

Net Income (Loss)

We reported a net income of \$410 in 2021 compared to net loss of \$124 in 2020, an increase of \$534, or 430.6%. Basic and diluted earnings per share were \$0.12 and \$-0.04 in 2021 and 2020, 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 \$6,713 and \$1,090 at December 31, 2021 and 2020, respectively. The increase was due to the fact that at December 31, 2021 we held the majority of available funds in assets defined as cash and cash equivalents. At December 31, 2020, we held the majority of available funds in assets defined as investments. Working capital was \$11,931 at December 31, 2021 compared to \$11,323 at December 31, 2020.

Cash generated from operating activities increased \$438 to \$769 in 2021 from \$331 in 2020. The increase was primarily due to an increase in net income, partially offset by net increases in trade receivables and inventories. The 2021 net income compared to the 2020 net loss was due to increased sales and gross margin. The increase in trade receivables was primarily due to increased net sales. The increase in inventories was due to the timing of inventory receipts. We are purchasing key components as they are available due to increased lead times and uncertainty of deliveries.

Cash generated from investing activities in 2021 was \$4,860, compared to cash used in investing activities \$8,020 in 2020. The increase in cash generated was due to a decrease in purchases of Treasury Bills classified as investments. In addition, we purchased \$141 and \$25 of property, equipment, and intangibles in 2021 and 2020, respectively.

Cash used in financing activities during 2021 and 2020 was \$6. The cash used was for principal payments on a financing lease on right-to-use assets.

Subject to the following section, entitled COVID-19 Pandemic Discussion, the Company believes its ongoing cash usage requirements will be primarily for capital expenditures, potential acquisitions, investments we believe present good opportunities for the Company and its shareholders, research and development, working capital, and growth initiatives. 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.

COVID-19 Pandemic Discussion

The COVID-19 pandemic continues to affect our operations, including limiting our ability to travel and fully engage customers at their facilities. While many regions of the US have reduced the severe restrictions implemented during 2020, many customers continue to operate under modified restrictions based on the number of COVID-19 cases. The uncertainty surrounding the ongoing fluctuations in regional case counts creates uncertainty in our business and may negatively affect our 2022 financial results.

We typically have robust sources for production components and materials. However, we are increasingly experiencing significant disruptions in our supply chain, resulting in difficulty sourcing parts. Additionally, we are experiencing substantial price increases for many of the components used in our products. In certain situations, we are modifying product designs to accommodate new components that are more readily available. There is no guarantee that we will continue to be successful in updating these designs and sourcing alternative components, and we could experience significant delays or run out of certain components and materials. We are also seeing delays in shipping and transportation services, which may adversely affect our ability to make timely deliveries to our customers. Furthermore, the labor market for qualified employees able to fill our production positions is challenging and may result in delays in filling open positions. While we continue to closely manage each of these activities, our actions may not be successful and may result in a negative effect on our sales and profit margins.

As of the date of this filing, we expect our business may be negatively affected but cannot currently determine the significance and duration of the pandemic on our business.

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 affect 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. Even though these equity securities were only valued at \$56 at December 31, 2021, changes in the value of these equity securities could affect our profitability as the value fluctuates. Any change in the value of these 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.

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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, 2021 and 2020 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, 2021, 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, 2021 and 2020, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2021, 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.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Revenue Recognition

Description of the Matter

As described in Note 1 to the financial statements, the Company recognizes revenue when control of the promised goods or services is transferred to customers, in an amount that reflects the consideration the Company expects to be entitled to in exchange for those goods or services.

The Company enters into certain contracts with its customers that may contain multiple performance obligations. Significant judgment may be required by the Company in determining revenue recognition specific to these contracts with multiple performance obligations, and includes the following:

- Determination of whether products and services are considered distinct performance obligations that should be accounted for separately or combined as one unit of accounting.
- Determination of stand-alone selling prices for each distinct performance obligation, particularly for products and services not sold separately.

Given these factors, the related audit effort in evaluating management's judgments in determining revenue recognition for these customer agreements was extensive and required a high degree of auditor judgment.

How We Addressed the Matter in Our Audit

Our audit procedures related to product sales included the following, among others:

- We evaluated the Company's accounting policies and related disclosures for compliance with applicable revenue recognition accounting guidance.
- We obtained an understanding of the design and implementation of internal controls related to the Company's revenue recognition process, including the identification of performance obligations and allocation of transaction price.
- We performed analytical procedures to test the reasonableness of recorded balances.
- We performed procedures to test the transactions were recorded in the appropriate accounting period.
- We performed a proof of cash analysis comparing cash receipts to revenue recognized through the year.

/s/ Boulay PLLP

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

Minneapolis, Minnesota

March 31, 2022

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

	December 31	
	2021	2020
ASSETS		
Current assets		
Cash and cash equivalents	\$ 6,713	\$ 1,090
Treasury Bills	3,000	7,999
Equity securities	56	42
Trade receivables, less allowance for doubtful accounts of \$11	1,005	957
Inventories	1,663	1,572
Other current assets	188	170
Income tax receivable	3	26
Total current assets	12,628	11,856
Deferred income tax asset	208	246
Intangible assets, net	38	228
Property and equipment, net	1,017	989
Total assets	\$ 13,891	\$ 13,319
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current maturity of financing lease	\$ 6	\$ 6
Accounts payable	349	197
Accrued expenses	342	330
Total current liabilities	697	533
Long-term liabilities		
Financing lease, net of current maturities	6	12
Total long-term liabilities	6	12
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	2,041	2,036
Retained earnings	10,808	10,398
Accumulated other comprehensive gain (unrealized gain on available-for-sale securities, net of income tax)	0	1
Total stockholders' equity	13,188	12,774
Total liabilities and stockholders' equity	\$ 13,891	\$ 13,319

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,	
	2021	2020
Net sales	\$ 8,607	\$ 7,621
Cost of goods sold	<u>3,930</u>	<u>3,691</u>
Gross profit	<u>4,677</u>	<u>3,930</u>
Operating expenses		
Selling and marketing	1,373	1,612
General and administrative	1,987	1,686
Research and development	<u>876</u>	<u>836</u>
Total operating expenses	<u>4,236</u>	<u>4,134</u>
Operating income (loss)	<u>441</u>	<u>(204)</u>
Non-operating income (expense)		
Interest expense	(1)	(3)
Interest income	5	36
Other income (expense)	<u>14</u>	<u>(1)</u>
Total non-operating income, net	<u>18</u>	<u>32</u>
Income (loss) before income taxes	<u>459</u>	<u>(172)</u>
Income tax expense (benefit)	<u>49</u>	<u>(48)</u>
Net income (loss)	<u>410</u>	<u>(124)</u>
Other comprehensive income (loss)		
Change in unrealized value of available-for-sale securities, net of income tax	<u>(1)</u>	<u>1</u>
Other comprehensive income (loss)	<u>(1)</u>	<u>1</u>
Net comprehensive income (loss)	<u>\$ 409</u>	<u>\$ (123)</u>
Net income (loss) per share data		
Basic		
Net income (loss) per share	<u>\$ 0.12</u>	<u>\$ (0.04)</u>
Weighted average shares	<u>3,395,521</u>	<u>3,395,521</u>
Diluted		
Net income (loss) per share	<u>\$ 0.12</u>	<u>\$ (0.04)</u>
Weighted average shares	<u>3,444,939</u>	<u>3,395,521</u>

See Notes to Financial Statements

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

	<u>Common Stock Issued</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total Stockholders' Equity</u>
	<u>Shares</u>	<u>Amount</u>				
Balance, December 31, 2019	3,395,521	\$ 339	\$ 2,030	\$ 10,522	\$ 0	\$ 12,891
Other comprehensive income					1	1
Stock-based compensation expense			6			6
Net loss				(124)		(124)
Balance, December 31, 2020	3,395,521	339	2,036	10,398	1	12,774
Other comprehensive loss					(1)	(1)
Stock-based compensation expense			5			5
Net income				410		410
Balance, December 31, 2021	<u>3,395,521</u>	<u>\$ 339</u>	<u>\$ 2,041</u>	<u>\$ 10,808</u>	<u>\$ 0</u>	<u>\$ 13,188</u>

See Notes to Financial Statements

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

	Years ended December 31,	
	2021	2020
Cash flows from operating activities		
Net income (loss)	\$ 410	\$ (124)
Adjustments to reconcile net income (loss) to net cash from operating activities:		
Depreciation and amortization	295	360
Deferred income taxes	38	(43)
Stock-based compensation expense	5	6
Interest accrued on Treasury Bills	(2)	(4)
Other	(7)	4
Change in:		
Trade receivables	(48)	79
Inventories	(91)	123
Other current assets	(18)	(11)
Accounts payable	152	68
Accrued expenses	12	(101)
Income taxes receivable	23	(26)
Net cash from operating activities	<u>769</u>	<u>331</u>
Cash flows from (used in) investing activities		
Purchases of Treasury Bills	(11,999)	(13,745)
Proceeds from the maturity of Treasury Bills	17,000	5,750
Purchase of property and equipment	(141)	(25)
Net cash from (used in) investing activities	<u>4,860</u>	<u>(8,020)</u>
Cash flows used in financing activities		
Payments on financing lease	(6)	(6)
Proceeds from Paycheck Protection Program	0	645
Repayment of Paycheck Protection Program loan	0	(645)
Net cash used in financing activities	<u>(6)</u>	<u>(6)</u>
Net increase (decrease) in cash and cash equivalents	5,623	(7,695)
Cash and cash equivalents, beginning	1,090	8,785
Cash and cash equivalents, ending	<u>\$ 6,713</u>	<u>\$ 1,090</u>
Supplemental cash flow information		
Cash paid during the year for income taxes	<u>\$ 15</u>	<u>\$ 20</u>
Cash paid during the year for interest	<u>\$ 1</u>	<u>\$ 3</u>

See Notes to Financial Statements

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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. 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, and stock compensation expense. 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.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

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 due 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, 2021, the Company had no customers that exceeded 10% of the accounts receivable balance. As of December 31, 2020, there were two customer that accounted for approximately 21% of the accounts receivable balance.

Investments

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 estimate of a 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 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. Equity securities with readily determinable values are stated at fair value. 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, 2021 and 2020.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

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 non-financial 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 non-financial 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 non-financial 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, 2021 and 2020 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

	<u>Years</u>
Autos	3
Equipment	5 - 10
Furniture and Fixtures	3 - 7
Building	7 - 40

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

Intangible assets

The intangible asset is a communication technology. The Company amortizes the cost of the intangible asset on a straight-line method over the estimated useful life. At December 31, 2020, the Company also had the HazardPRO technology which was fully amortized in the 2021 third quarter.

Revenue recognition

At contract inception, the Company assesses the goods and services to be provided to a customer and identifies a performance obligation for each distinct 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 to be provided 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. Certain contracts 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 \$40 and \$45 in 2021 and 2020, respectively.

Research and development

Expenditures for research and development are expensed as incurred. The Company incurred expenses of \$876 and \$836 in 2021 and 2020, 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 have a valuation allowance on our deferred tax asset of \$220 and \$186 at December 31, 2021 and 2020 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.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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 were exercised or converted into common stock. For the years ending December 31, 2021 and 2020, respectively, options to purchase 283,082 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).

	<u>Income (loss)</u>	<u>Shares</u>	<u>Per share amount</u>
2021:			
Basic EPS	\$ 410	3,395,521	\$ 0.12
Effect of dilutive stock options		49,418	0.00
Diluted EPS	<u>\$ 410</u>	<u>3,444,939</u>	<u>\$ 0.12</u>
2020:			
Basic EPS	\$ (124)	3,395,521	\$ (0.04)
Effect of dilutive stock options		0	0.00
Diluted EPS	<u>\$ (124)</u>	<u>3,395,521</u>	<u>\$ (0.04)</u>

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, 2021, the Company had two stock-based compensation plans.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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 original terms ranging from one month to eight months. Treasury Bills with an original maturity date of three months or less are included within cash and cash equivalents on the balance sheet at December 31, 2021.

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.

Equity securities are measured at fair value and unrealized gains and losses are recognized in non-operating income.

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

	Cost	Gross unrealized gain	Gross unrealized loss	Fair value
December 31, 2021				
Commercial Paper	\$ 1,520	\$ 0	\$ 0	\$ 1,520
Treasury Bills	8,000	0	0	8,000
Equity Securities	54	2	0	56
	<u>9,574</u>	<u>2</u>	<u>0</u>	<u>9,576</u>
Less Cash Equivalents	6,520	0	0	6,520
Total Investments, December 31, 2021	<u>\$ 3,054</u>	<u>\$ 2</u>	<u>\$ 0</u>	<u>\$ 3,056</u>
December 31, 2020				
Commercial Paper	\$ 718	\$ 0	\$ 0	\$ 718
Treasury Bills	7,998	1	0	7,999
Equity Securities	54	0	(12)	42
	<u>8,770</u>	<u>1</u>	<u>(12)</u>	<u>8,759</u>
Less Cash Equivalents	718	0	0	718
Total Investments, December 31, 2020	<u>\$ 8,052</u>	<u>\$ 1</u>	<u>\$ (12)</u>	<u>\$ 8,041</u>

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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,	
	2021	2020
Unrealized Gains		
Unrealized holding gains arising during the period	\$ 0	\$ 1
Less: Reclassification of gains included in net income (loss)	(1)	0
	(1)	1
Deferred Taxes on Unrealized Gains:		
Increase in deferred taxes on unrealized gains arising during the period	0	0
Less: Reclassification of taxes on gains included in net income (loss)	0	0
	0	0
Net Change in Accumulated Other Comprehensive Income (Loss)	\$ (1)	\$ 1

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, 2021

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using		
			Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents:					
Commercial paper	\$ 1,520	\$ 1,520	\$ 1,520	\$ 0	\$ 0
Treasury Bills	5,000	5,000	5,000	0	0
Treasury Bills - maturity date greater than three months	3,000	3,000	3,000	0	0
Equity securities	56	56	0	0	56

December 31, 2020

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using		
			Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents:					
Commercial paper	\$ 718	\$ 718	\$ 718	\$ 0	\$ 0
Treasury Bills	7,999	7,999	7,999	0	0
Equity securities	42	42	0	0	42

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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 equity securities owned by the Company are investments in two non-publicly traded companies, as a previously owned non-publicly traded company spun off its wholly owned subsidiary in October 2020. Each shareholder in the parent company received the same number of shares in the spun off new company. There is an undeterminable market for each of these two companies 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:

	<u>Years Ended December 31,</u>	
	<u>2021</u>	<u>2020</u>
Beginning Balance	\$ 42	\$ 45
Change in value	14	(3)
Ending Balance	<u>\$ 56</u>	<u>\$ 42</u>

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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,	
	2021	2020
Raw Materials	\$ 1,129	\$ 922
Work In Process	257	292
Finished Goods	287	363
Reserve for Obsolescence	(10)	(5)
Total Inventories	\$ 1,663	\$ 1,572

Note 5. Property and Equipment, Net

The following is a summary of property and equipment:

	December 31,	
	2021	2020
Autos	\$ 23	\$ 23
Equipment	300	302
Furniture and Fixtures	485	501
Right-of-Use Asset	30	30
Building	1,373	1,382
Land	415	415
	2,626	2,653
Less Accumulated Depreciation	1,609	1,664
Total Property and Equipment	\$ 1,017	\$ 989

Depreciation expense for the years ended December 31, 2021 and 2020 was \$105 and \$99, respectively.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

Note 6. Net Intangible Assets

Intangible assets include the following:

	Average Useful Lives	December 31, 2021		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Technology	7 Years	\$ 1,478	\$ 1,478	\$ 0
Communication Technology	3 Years	150	112	38
Net Intangible Assets		\$ 1,628	\$ 1,590	\$ 38

	Average Useful Lives	December 31, 2020		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Technology	7 Years	1,478	1,337	141
Communication Technology	3 Years	150	63	87
Net Intangible Assets		\$ 1,628	\$ 1,400	\$ 228

Amortization expense for the years ended December 31, 2021 and 2020 was \$190 and \$261, respectively.

Estimated amortization expense in 2022 is \$38.

Note 7. Accrued Expenses

Accrued expenses include the following:

	December 31,	
	2021	2020
Wages and Commissions	\$ 281	\$ 257
Other	61	73
Total Accrued Expenses	\$ 342	\$ 330

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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 two years at December 31, 2021.

The components of lease expense were as follows:

	<u>Years Ended December 31,</u>	
	<u>2021</u>	<u>2020</u>
Finance lease cost:		
Amortization of right-of-use assets	\$ 6	\$ 6
Interest on lease liabilities	1	1
Total finance lease cost	<u>\$ 7</u>	<u>\$ 7</u>

Supplemental balance sheet information related to leases is as follows:

	<u>December 31,</u>	
	<u>2021</u>	<u>2020</u>
Finance leases		
Property and equipment, gross	\$ 30	\$ 30
Accumulated amortization	(19)	(13)
Property and equipment, net	<u>\$ 11</u>	<u>\$ 17</u>
Weighted average remaining lease term		
Finance leases		2 years
Weighted average discount rate		
Finance leases		7.0%

Maturities of lease liabilities are as follows:

Year ending December 31	
2022	\$ 7
2023	6
Total lease payments	13
Less amount representing interest	(1)
Total	<u>\$ 12</u>

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
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(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, 2021, options to purchase an aggregate of 325,000 shares were outstanding under the 2013 Plan, of which options to purchase 320,000 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, 2021, 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 the years ended December 31, 2021 and 2020.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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:

	<u>Options Outstanding</u>			
	<u>Number of Shares</u>	<u>Weighted- Average Exercise Price</u>	<u>Weighted- Average Remaining Contractual Term (in years)</u>	<u>Aggregate Intrinsic Value (1)</u>
Balance at December 31, 2019	125,000	\$ 3.78	7.1	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2020	125,000	3.78	6.1	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2021	<u>125,000</u>	<u>\$ 3.78</u>	<u>5.1</u>	
Vested and exercisable as of December 31, 2021	<u>120,000</u>			<u>\$ 300</u>

(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, 2021.

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

	<u>Options Outstanding</u>			
	<u>Number of Shares</u>	<u>Weighted- Average Exercise Price</u>	<u>Weighted- Average Remaining Contractual Term (in years)</u>	<u>Aggregate Intrinsic Value (1)</u>
Balance at December 31, 2019	207,500	\$ 4.62	3.4	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2020	207,500	4.62	2.4	
Granted	0			
Exercised	0			
Canceled/forfeited/expired	0			
Balance at December 31, 2021	<u>207,500</u>	<u>\$ 4.62</u>	<u>1.4</u>	
Vested and exercisable as of December 31, 2021	<u>207,500</u>			<u>\$ 345</u>

(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, 2021.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

The Company recognized compensation expense in connection with the issuance of options of approximately \$5 and \$6 during the years ended December 31, 2021 and 2020, respectively.

There were no options exercised during the years ended December 31, 2021 and 2020.

As of December 31, 2021, there was approximately \$4 of unrecognized compensation expense under the 2013 Plan. The Company expects to recognize this expense over the next year. 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, 2021. All shares held by the ESOP have been released and allocated to participants' accounts. No dividends were paid during the years ended December 31, 2021 and 2020. The ESOP had no debt to the Company at December 31, 2021 or 2020.

The Company recognized compensation expense for contributions of \$30 and \$24 to the ESOP plan for the years ended December 31, 2021 and 2020, respectively.

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, 2021, 135,490 shares of the Company’s stock, with an aggregate fair market value of approximately \$851, 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 because its stock is listed on the Nasdaq Capital Market it meets the ESOP requirements and that there would not be a current obligation for it to repurchase any distributed ESOP 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 2021 or 2020.

ELECTRO-SENSORS, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(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, 2021 and 2020 are as follows:

	<u>2021</u>	<u>2020</u>
Current:		
Federal	\$ 10	\$ (6)
State	1	1
Deferred:		
Federal	38	(43)
State	0	0
Total Federal and State Income Taxes	<u>\$ 49</u>	<u>\$ (48)</u>

The provision for income taxes for the years ended December 31, 2021 and 2020 differs from the amount obtained by applying the U.S. federal income tax rate to pretax income due to the following:

	<u>2021</u>	<u>2020</u>
Computed "Expected" Federal Tax Expense (Benefit From)	\$ 96	\$ (36)
Increase (Decrease) in Taxes Resulting From:		
State Income Taxes, net of Federal Benefit	1	1
R&D Credits	(99)	(7)
Permanent Differences	4	1
Other	47	(7)
Total Federal and State Income Taxes	<u>\$ 49</u>	<u>\$ (48)</u>

ELECTRO-SENSORS, INC. AND SUBSIDIARIES
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2021 AND 2020
(in thousands except share and per share amounts)

The components of the net deferred tax asset consist of:

	2021	2020
Deferred Tax Assets:		
Vacation accrual	\$ 27	\$ 29
Allowance for doubtful accounts	2	2
Stock compensation	96	94
Bonus	4	0
Depreciation and amortization	100	94
Inventory Obsolescence	2	1
R&D credit carryforward	220	235
Valuation allowance	(220)	(186)
Total Deferred Tax Assets	231	269
Deferred Tax Liabilities:		
Prepaid expenses	23	23
Total Deferred Tax Liabilities	23	23
Net Deferred Tax Asset	\$ 208	\$ 246

R&D credits can be carried forward for twenty years for federal purposes and fifteen years in Minnesota.

The Company is materially subject to the following taxing jurisdictions: U.S. and Minnesota. The tax years 2018 through 2020 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, 2021 or December 31, 2021 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, 2021 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, 2021. 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, 2021.

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 2021 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.

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 "2022 Proxy Statement") for its Annual Meeting of Shareholders to be held April 20, 2022 ("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 2022 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), if any, will be set forth under the caption "Delinquent Section 16(a) Reports" in the 2022 Proxy Statement and is incorporated herein by reference. If there are no Delinquent Section 16(a) Reports required, this section will be omitted from the 2022 Proxy Statement.

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 2022 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 2022 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 2022 Proxy Statement and is incorporated herein by reference.

The following table provides information as of December 31, 2021 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 2022 Proxy Statement and is incorporated herein by reference.

The information required by Item 407(a) will be set forth in the 2022 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 2022 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 16 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, incorporated by reference to Exhibit 3.2 to the Form 10-K for the year ended December 31, 2020
4.1	Description of the Registrant's Securities Registered Pursuant to Section 12 of the Securities Exchange Act of 1934, incorporated by reference to Exhibit 4.1 to the Form 10-K for the year ended December 31, 2019
*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 31, 2022
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, 2021, formatted in iXBRL (Inline eXtensible Business Reporting Language): (i) Balance Sheets as of December 31, 2021 and 2020, (ii) Statements of Comprehensive Income (Loss) for the years ended December 31, 2021 and 2020, (iii) Statements of Cash Flows for years ended December 31, 2021 and 2020, (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 10-K 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 31, 2022

By: /s/ GLORIA M. GRUNDHOEFER

Gloria M. Grundhoefer

Controller

Date: March 31, 2022

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.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
/s/David L. Klenk	President and Director (CEO and CFO)	March 31, 2022
/s/ Joseph A. Marino	Chairman and Director	March 31, 2022
/s/ Scott A. Gabbard	Director	March 31, 2022
/s/ Michael C. Zipoy	Director	March 31, 2022
/s/ Jeffrey D. Peterson	Director	March 31, 2022



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 31, 2022 relating to the financial statements that appear in this Annual Report on Form 10-K for the year ended December 31, 2021.

/s/ Boulay PLLP
Minneapolis, MN
March 31, 2022

**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 31, 2022

/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 Annual Report of Electro-Sensors, Inc. (the "Company") on Form 10-K for the year ended December 31, 2021 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 31, 2022

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

March 31, 2022

Dear Shareholders:

Welcome to the 2021 Electro-Sensors Annual Report. We appreciate your interest in the company as we continue to deliver industry-leading machine monitoring sensors and hazard monitoring systems for global industrial and agricultural applications. For over 50 years, our customers have relied on us to provide innovative and cost-effective solutions, enabling efficient factory automation while helping to create increasingly safe work environments. Our customers trust us to protect their most valuable assets - their people and facilities - and our amazing employees eagerly rise to this challenge!

The year was noteworthy as we emerged from the depth of the COVID-19 pandemic and its many constraints. Business conditions are improving and will eventually return to pre-pandemic norms. We are particularly excited to be able to travel once again and meet face to face with our customers. We are grateful to our customers for their patience and partnership throughout these trying times, and proud of our employees for their commitment and persistence in the face of these challenges.

We are pleased to report that in 2021 we achieved record annual revenue of \$8.6 million, up 12.9% from the previous year. This growth was driven by customers moving forward with both capacity upgrades and facility modernization plans after pausing some of these initiatives during the pandemic. Additionally, gross profit improved to 54.3%, up from 51.6% in the prior year, as we drove higher levels of efficiency to support our increased revenue.

These favorable results were achieved despite significant challenges associated with our supply chain. Many generally available components used in our products are now regularly out of stock or quoted with extremely long lead times. Furthermore, we are experiencing significant inflationary pressure that has driven up component and raw material prices. Although we are uncertain how long this unbalanced supply environment will persist, and how it may impact our ability to fulfill customer orders in a timely manner, we will continue to actively pursue all avenues for sourcing parts and identifying suitable substitutes as required.

While 2022 appears to have its own set of challenges, including an ongoing conflict in Europe, we are thankful to have the pandemic significantly behind us and we remain encouraged with customer activity and the favorable demand to our products. Electro-Sensors is built on an enduring foundation that is well positioned to adapt to these changing dynamics. By staying close to our customers and continuing to deliver the robust products and thoughtful services for which we are famous, we believe we will continue to expand our reach and engage new and meaningful market opportunities.

Thanks again for your continued support of Electro-Sensors. Similar to last year, we will be conducting a virtual annual shareholder meeting on April 20, 2022. Please see your proxy statement or visit our website (www.electro-sensors.com) for details on how to access and participate in the virtual meeting.

Sincerely,



David Klenk

INVESTOR INFORMATION

Annual Meeting

The Annual Meeting of Shareholders will be held at www.virtualshareholdermeeting.com/ELSE2022 on April 20, 2022 at 2:00 p.m. Central time. 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 PLLP
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**