BALLANTYNE OF OMAHA INC
Form 10-Q
May 15, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

ý	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the quarterly period ended March 31, 2006
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	For the transition period from to
	Commission File Number: 1-13906

BALLANTYNE OF OMAHA, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**47-0587703** (IRS Employer Identification Number)
4350 McKinley Street, Omaha, Nebraska (Address of Principal Executive Offices)	**68112** Zip Code

(402) 453-4444

Registrant s telephone number, including area code:

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding twelve 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 ý No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer ý

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

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

Class	**Outstanding as of May 12, 2006**
Common Stock, $.01, par value	13,542,531 shares

TABLE OF CONTENTS

Part I. Financial Information

Item 1. Financial Statements

Ballantyne of Omaha, Inc. and Subsidiaries

Consolidated Balance Sheets

March 31, 2006 and December 31, 2005

		March 31, 2006 (Unaudited)		December 31, 2005
Assets				
Current assets:				
Cash and cash equivalents	$	22,049,763	$	19,628,348
Accounts receivable (less allowance for doubtful accounts of $440,943 in 2006 and $420,223 in 2005)		6,587,272		7,821,085
Inventories, net		11,209,687		9,942,065
Deferred income taxes		1,354,818		1,247,609
Other current assets		349,434		430,411
Total current assets		41,550,974		39,069,518
Property, plant and equipment, net		5,218,775		5,379,933
Goodwill, net		2,467,219		2,467,219
Other assets		19,257		19,257
Total assets	$	49,256,225	$	46,935,927
Liabilities and Stockholders Equity				
Current liabilities:				
Current portion of long-term debt	$	28,239	$	27,761
Accounts payable		3,494,727		2,212,056
Warranty reserves		690,162		680,017
Accrued group health insurance claims		190,836		275,468
Accrued bonuses		42,621		983,235
Other accrued expenses		2,155,215		1,663,708
Customer deposits		374,681		536,724
Income tax payable		515,022		63,217
Total current liabilities		7,491,503		6,442,186
Long-term debt, net of current portion		7,367		14,609
Deferred income taxes		118,574		156,912
Other accrued expenses, net of current portion		328,800		324,715
Total liabilities		7,946,244		6,938,422
Commitments and contingencies				
Stockholders equity:				
Preferred stock, par value $.01 per share; Authorized 1,000,000 shares, none outstanding				
Common stock, par value $.01 per share; Authorized 25,000,000 shares; issued 15,627,836 shares in 2006 and 15,495,336 shares in 2005		156,278		154,953
Additional paid-in capital		33,807,416		33,411,013
Retained earnings		22,661,741		21,746,993
		56,625,435		55,312,959
Less 2,097,805 common shares in treasury, at cost		(15,315,454)		(15,315,454)
Total stockholders equity		41,309,981		39,997,505
Total liabilities and stockholders equity	$	49,256,225	$	46,935,927

See accompanying notes to consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries

Consolidated Statements of Operations

Three Months Ended March 31, 2006 and 2005

(Unaudited)

	2006	2005
Net revenues	$ 12,433,338	$ 12,511,869
Cost of revenues	9,102,371	9,117,278
Gross profit	3,330,967	3,394,591
Selling and administrative expenses:		
Selling	734,523	739,412
Administrative	1,369,684	1,194,412
Total selling and administrative expenses	2,104,207	1,933,824
Income from operations	1,226,760	1,460,767
Interest income	166,185	72,152
Interest expense	(8,022)	(8,656)
Other income (expense), net	18,880	(29,519)
Income before income taxes	1,403,803	1,494,744
Income tax expense	(489,055)	(552,830)
Net income	$ 914,748	$ 941,914
Basic earnings per share	$ 0.07	$ 0.07
Diluted earnings per share	$ 0.07	$ 0.07
Weighted average shares outstanding:		
Basic	13,440,500	13,050,733
Diluted	13,947,291	13,840,719

See accompanying notes to consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

Three Months Ended March 31, 2006 and 2005

(Unaudited)

	2006	2005
Cash flows from operating activities:		
Net income	$ 914,748	$ 941,914
Adjustments to reconcile net income to net cash provided by operating activities.		
Provision for doubtful accounts	18,750	(69,301)
Depreciation of property, plant and equipment	279,934	281,405
Other amortization		10,066
Deferred income taxes	(145,547)	14,360
Share-based compensation	31,723	
Excess tax benefits from stock options exercised	(180,397)	
Changes in assets and liabilities:		
Accounts receivable	1,215,063	493,592
Inventories	(1,267,622)	(257,400)
Other current assets	80,977	125,296
Accounts payable	1,282,671	546,334
Warranty reserves	10,145	8,212
Accrued group health insurance claims	(84,632)	(28,088)
Accrued bonuses	(940,614)	(628,878)
Other accrued expenses	487,650	159,279
Customer deposits	(162,043)	(122,207)
Current income taxes	632,202	476,069
Other assets		1,500
Net cash provided by operating activities	2,173,008	1,952,153
Cash flows from investing activities:		
Capital expenditures	(118,776)	(83,020)
Net cash used in investing activities	(118,776)	(83,020)
Cash flows from financing activities:		
Payments on long-term debt	(6,764)	(6,321)
Proceeds from exercise of stock options	193,550	224,625
Excess tax benefits from stock options exercised	180,397	
Net cash provided by financing activities	367,183	218,304
Net increase in cash and cash equivalents	2,421,415	2,087,437
Cash and cash equivalents at beginning of period	19,628,348	14,031,984
Cash and cash equivalents at end of period	$ 22,049,763	$ 16,119,421

See accompanying notes to consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Three Months Ended March 31, 2006 and 2005

(Unaudited)

1. Company

Ballantyne of Omaha, Inc., a Delaware corporation (Ballantyne or the Company), and its wholly-owned subsidiaries Strong Westrex, Inc., and Design & Manufacturing, Inc., design, develop, manufacture and distribute commercial motion picture equipment and lighting systems and distribute restaurant products. The Company s products are distributed to movie exhibition companies, sports arenas, auditoriums, amusement parks, special venues, and the food service industry. Refer to the Business Segment Section (note 11) for further information.

2. Summary of Significant Accounting Policies

The principal accounting policies upon which the accompanying consolidated financial statements are based are summarized as follows:

a. Basis of Presentation and Principles of Consolidation

The consolidated financial statements included herein are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America for annual reporting purposes or those made in the Company s annual Form 10-K filing. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Form 10-K for fiscal 2005.

In the opinion of management, the unaudited consolidated financial statements of the Company reflect all adjustments of a normal recurring nature necessary to present a fair statement of the financial position and the results of operations and cash flows for the respective interim periods. The results for interim periods are not necessarily indicative of trends or results expected for a full year.

b. Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results and changes in facts and circumstances may alter such estimates and affect results of operations and financial position in future periods.

c. Allowance for Doubtful Accounts

Accounts receivable are presented net of allowance for doubtful accounts of $440,943 and $420,223 at March 31, 2006 and December 31, 2005, respectively. This allowance is developed based on several factors including overall customer credit quality, historical write-off experience and a specific analysis that projects the ultimate collectibility of the account. As such, these factors may change over time causing the reserve level to adjust accordingly.

d. Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market and include appropriate elements of material, labor and manufacturing overhead. Inventory balances are net of reserves of slow moving or obsolete inventory estimated based on management s review of inventories on hand compared to estimated future usage and sales.

e. Goodwill

The Company capitalizes and includes in intangible assets the excess of cost over the fair value of net identifiable assets of operations acquired through purchase transactions (goodwill) in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 142 requires goodwill no longer be amortized to earnings, but instead be reviewed at least annually for impairment. An impairment loss is recognized to the extent that the carrying amount exceeds the asset s estimated fair value.

f. Property, Plant and Equipment

Significant expenditures for the replacement or expansion of property, plant and equipment are capitalized. Depreciation of property, plant and equipment is provided over the estimated useful lives of the respective assets using the straight-line method. For financial reporting purposes, assets are depreciated over the estimated useful lives of 20 years for buildings and improvements, 3 to 10 years for machinery and equipment, 7 years for furniture and fixtures and 3 years for computers and accessories. The Company generally uses accelerated methods of depreciation for income tax purposes.

g. Income Taxes

Income taxes are accounted for under the asset and liability method. The Company uses an estimate of its annual effective rate at each interim period based on the facts and circumstances at the time while the actual effective rate is calculated at year-end. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized.

h. Revenue Recognition

The Company recognizes revenue from product sales upon shipment to the customer when collectibility is reasonably assured. Revenues related to services are recognized as earned over the terms of the contracts or delivery of the service to the customer.

The Company enters into transactions that represent multiple element arrangements, which may include a combination of services and asset sales. Under EITF 00-21, *Revenue Arrangements with Multiple Deliverables*, multiple element arrangements are assessed to determine whether they can be separated into more than one unit of accounting. A multiple element arrangement is separated into more than one unit of accounting if all of the following criteria are met.

The delivered item(s) has value on a standalone basis;

There is objective and reliable evidence of the fair value of the undelivered item(s);

If the arrangement includes a general right of return relative to the delivered item(s), delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company.

If these criteria are not met, then revenue is deferred until such criteria are met or until the period(s) over which the last undelivered element is delivered. If there is objective and reliable evidence of fair value for all units of accounting in an arrangement, the arrangement consideration is allocated to the separate units of accounting based on each unit s relative fair value. There may be cases, however, in which there is objective and reliable evidence of fair value of the undelivered item(s) but no such evidence for the delivered item(s). In those cases, the residual method is used to allocate the arrangement consideration. Under the residual method, the amount of consideration allocated to the delivered item(s) equals the total arrangement consideration less the aggregate fair value of the undelivered item.

i. Fair Value of Financial Instruments

The fair value of a financial instrument is the amount at which the instruments could be exchanged in a current transaction between willing parties. All financial instruments reported in the consolidated balance sheets equal or approximate their fair values.

j. Cash and Cash Equivalents

All highly liquid financial instruments with maturities of three months or less from date of purchase are classified as cash equivalents in the consolidated balance sheets and statements of cash flows.

k. Earnings Per Common Share

The Company computes and presents earnings per share in accordance with SFAS No. 128, *Earnings Per Share*. Basic earnings per share has been computed on the basis of the weighted average number of shares of common stock outstanding. Diluted earnings per share has been computed on the basis of the weighted average number of shares of common stock outstanding after giving effect to potential common shares from dilutive stock options. The following table provides a reconciliation between basic and diluted earnings per share:

	Three Months Ended March 31,	
	2006	**2005**
Basic earnings per share:		
Earnings applicable to common stock	$ 914,748	$ 941,914
Weighted average common shares outstanding	13,440,500	13,050,733
Basic earnings per share	$ 0.07	$ 0.07

Diluted earnings per share:				
Earnings applicable to common stock	$	914,748	$	941,914
Weighted average common shares outstanding		13,440,500		13,050,733
Assuming conversion of options outstanding		506,791		789,986
Weighted average common shares outstanding, as adjusted		13,947,291		13,840,719
Diluted earnings per share	$	0.07	$	0.07

At March 31, 2006, options to purchase 286,733 shares of common stock at a weighted average price of $8.15 per share were outstanding, but were not included in the computation of diluted earnings per share for the three months ended March 31, 2006 as the options exercise price was greater than the average market price of the common shares. These options expire between January 2007 and May 2010. At March 31, 2005, options to purchase 197,925 shares of common stock at a weighted average price of $9.74 per share were outstanding, but were not included in the computation of diluted earnings per share for the three months ended March 31, 2005.

l. Share-Based Payments

Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123R (SFAS 123R), Share-Based Payments, which requires the measurement and recognition of compensation expense for all share-based payment awards to employees and directors based on estimated fair values. SFAS 123R supersedes the Company s previous accounting methodology using the intrinsic value method under Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees. Under the intrinsic value method, no share-based compensation expense related to stock option awards granted to employees had been recognized in the Company s consolidated statements of operations, as all stock option awards granted under the plans had an exercise price equal to the market value of the common stock on the date of the grant.

The Company adopted SFAS 123R using the modified prospective transition method. Under this transition method, compensation expense recognized during the three months ended March 31, 2006 included: (a) compensation expense for all share-based awards granted prior to, but not yet vested, as of December 31, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation expense for all share-based awards granted subsequent to December 31, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. The Company did not grant options during the three months ended March 31, 2006. In accordance with the modified prospective transition method, the Company s consolidated financial statements for prior periods have not been restated to reflect the impact of SFAS 123R.

On November 10, 2005 the Financial Accounting Standards Board (FASB) issued FASB Staff Position No. 123R-3, Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards. The Company has elected to adopt the alternative transition method provided in the FASB Staff Position for calculating the tax effects of share-based compensation pursuant to SFAS 123R. The alternative transition method includes simplified methods to establish the beginning balance of the additional paid-in capital pool (APIC Pool) related to the tax effects of employee share-based compensation, and to determine the subsequent impact on the APIC Pool and consolidated statements of cash flows of the tax effects of employee and director share-based awards that are outstanding upon adoption of SFAS 123R.

Options

The Company currently has a 2001 Non-Employee Directors Stock Option Plan (2001 Directors Plan) and a 2005 Outside Directors Stock Option Plan (2005 Outside Directors Plan) which have been approved by the Company s stockholders. The Company also had a 1995 Employee Stock Option Plan and a 1995 Directors Stock Plan which expired in 2005, however, there are outstanding stock options under these two expired plans.

All past and future grants under the Company s stock option plans are granted at prices based on the fair market value of the Company s common stock on the date of grant. The outstanding options generally vest over periods ranging from zero to three years from the grant date and expire between 5 and 10 years.

7

No options have been granted under the 2005 Outside Directors Plan and all options granted under the 2001 Directors Plan and the 1995 Employee Stock Option Plan were fully vested, based on their original terms, prior to January 1, 2006. As such, no compensation expense related to those options has been recognized under SFAS 123R. The 1995 Outside Directors Stock Plan had 47,250 shares outstanding not yet vested at January 1, 2006 and were subject to the recognition of compensation expense.

A total of 1,152,940 shares of common stock have been reserved for issuance pursuant to the Company s stock option plans at March 31, 2006.

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 option-pricing model. The Company uses historical data among other factors to estimate the expected price volatility, the expected option life and the expected forfeiture rate. The risk-free rate is based on the U.S. Treasury yield in effect at the time of grant for the estimated life of the option. The Company has not and is not expected to pay cash dividends in the future. The Company did not grant stock options during the three months ended March 31, 2006 and 2005.

The following table summarizes the Company s activities with respect to its stock options for the first three months of 2006 as follows:

	Number of Shares		Weighted Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term		Aggregate Intrinsic Value
Outstanding at January 1, 2006	987,078	$	2.86			
Exercised	(132,500)	$	1.46			
Forfeited		$				
Outstanding at March 31, 2006	854,578	$	3.08	3.73	$	2,208,023
Exercisable at March 31, 2006	807,328	$	2.98	3.71	$	2,208,023

The total intrinsic value for options exercised during the three months ended March 31, 2006 and 2005 was $563,145 and $550,373, respectively. As of March 31, 2006, the total unrecognized compensation cost related to non-vested stock option awards was approximately $53,011 and is expected to be recognized over a weighted average period of 14 months.

Cash received from option exercises under all plans for the three months ended March 31, 2006 and 2005 was approximately $193,550 and $224,625, respectively. The actual tax benefit realized for the tax deductions from option exercises under all plans totaled approximately $180,397 and $189,186, respectively, for three months ended March 31, 2006 and 2005.

Restricted Stock Plan

During 2005, the Company adopted and the stockholders approved, the 2005 Restricted Plan. Under terms of the plan, the compensation committee of the Board of Directors selects which employees of the Company are to receive restricted stock awards and the terms of such awards. The total number of shares reserved for issuance under the plan is 250,000 shares. There have been no shares issued under the plan through March 31, 2006. The plan expires in September 2010.

8

Employee Stock Purchase Plan

The Company s Employee Stock Purchase Plan, approved by the stockholders, provides for the purchase of shares of Ballantyne common stock by eligible employees at a per share purchase price equal to 85% of the fair market value of a share of Ballantyne common stock at either the beginning or end of the offering period, as defined, whichever is lower. Purchases are made through payroll deductions of up to 10% of each participating employee s salary. The number of shares that can be purchased by participants in any offering period is 2,000 shares. Additionally, the Plan has set certain limits, as defined, in regard to the number of shares that may be purchased by all eligible employees during an offering period. At March 31, 2006, 150,000 shares of common stock remained available for issuance under the Plan. The Plan expires in September 2010. The total estimated grant date fair value of purchase rights outstanding under the Employee Stock Purchase Plan was $2.07 using the Black-Scholes option-pricing model made with the following weighted average assumptions: risk-free interest rate 4.31%; dividend yield 0%; expected volatility 43.4% and expected life in years 1. At March 31, 2006, total unrecognized estimated compensation cost was $29,159 which is expected to be recognized over a period of 7 months.

Share-Based Compensation Expense

The table below shows the amounts recognized in the financial statements for the three months ended March 31, 2006 for share-based compensation related to employees and directors.

		Three Months Ended March 31, 2006
Total cost of share-based compensation included in selling and administrative expenses, before income tax	$	31,723
Amount of income tax benefit recognized		(9,240)
Amount charged against net income	$	22,483
Impact on earnings share:		
Basic	$	(0.00)
Diluted	$	(0.00)

There were no amounts relating to share-based compensation capitalized in inventory during the three months ended March 31, 2006.

Pro Forma Share-Based Compensation Expense

Prior to December 31, 2005, the Company accounted for share-based compensation arrangements in accordance with the provisions and related interpretations of APB 25. Had compensation cost for share-based awards been determined consistent with SFAS No. 123R, the net income and earnings per share would have been adjusted to the following pro forma amounts:

		Three Months Ended March 31, 2005
Net income, as reported	$	941,914
Deduct: Total share-based compensation expense determined under fair value based method for all awards, net of related tax effects		(37,595)
Pro forma net income	$	904,319
Earnings per share:		
Basic-as reported	$	0.07
Basic-pro forma	$	0.07
Diluted-as reported	$	0.07
Diluted-pro forma	$	0.07

m. Impairment of Long-Lived Assets

The Company reviews long-lived assets, exclusive of goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

The Company s most significant long-lived assets subject to these periodic assessments of recoverability are property, plant and equipment, which have a net book value of $5.2 million at March 31, 2006. Because the recoverability of property, plant and equipment is based on estimates of future undiscounted cash flows, these estimates may vary due to a number of factors, some of which may be outside of management s control. To the extent that the Company is unable to achieve management s forecasts of future income, it may become necessary to record impairment losses for any excess of the net book value of property, plant and equipment over its fair value.

n. Warranty Reserves

The Company generally grants a warranty to its customers for a one-year period following the sale of all new equipment, and on selected repaired equipment for a one-year period following the repair. The warranty period is extended under certain circumstances and for certain products. The Company accrues for these costs at the time of sale or repair, when events dictate that additional accruals are necessary.

The following table summarizes warranty activity for the periods indicated below:

	Three Months Ended March 31, 2006		Three Months Ended March 31, 2005	
Balance at beginning of period	$	680,017	$	668,268
Charged to expense		57,750		69,245
Amounts written off, net of recoveries		(47,605)		(61,033)
Balance at end of period	$	690,162	$	676,480

o. Comprehensive Income

The Company s comprehensive income consists solely of net income. All other items were not material to the consolidated financial statements.

p. Litigation

During March 2006, Ballantyne settled an asbestos case entitled *Bercu v. BICC Cables Corporation, et al.*, originally filed June 27, 2003 in the Supreme Court of the State of New York. The settlement amount was not material to the Company s results of operations, financial position or cash flows.

Ballantyne is a party to various other legal actions which are ordinary routine litigation matters incidental to the Company s business, such as products liability. Based on currently available information, management believes that the ultimate outcome of these matters individually and in the aggregate, will not have a material adverse effect on the Company s results of operations, financial position or cash flows.

q. Environmental

The Company is subject to various federal, state and local laws and regulations pertaining to environmental protection and the discharge of material into the environment. During 2001, Ballantyne was informed by a neighboring company of likely contaminated soil on certain parcels of land adjacent to Ballantyne s main manufacturing facility in Omaha, Nebraska. The Environmental Protection Agency and the Nebraska Health and Human Services System subsequently determined that certain parcels of Ballantyne property had various levels of contaminated soil relating to a former pesticide company which previously owned the property and that burned down in the 1960 s. During October 2004, Ballantyne agreed to enter into an Administrative Order on Consent (AOC) to resolve the matter. The AOC holds Ballantyne and two other parties jointly and severally responsible for the cleanup. In this regard, the three parties have also entered into a Site Allocation Agreement by which they will divide past, current and future costs of the EPA, the costs of remediation and the cost of long term maintenance. In connection with the AOC, the Company has paid its share of the costs. At March 31, 2006, the Company has provided for management s estimate of any future payments relating to this matter which is not material to the consolidated financial statements.

r. Concentrations

The Company s top ten customers accounted for approximately 55% of 2006 consolidated net revenues. Trade accounts receivable from these customers represented approximately 62% of net consolidated receivables at March 31, 2006. Sales to AMC Theatres, Inc. and Regal Cinema, Inc. each represented over 10% of consolidated revenues. In addition, receivables from Vari International represented approximately 27% of net consolidated receivables at March 31, 2006. While the Company believes its relationships with such customers are stable, most arrangements are made by purchase order and are terminable at will by either party. A significant decrease or interruption in business from the Company s significant customers could have a material adverse effect on the Company s business, financial condition and results of operations. The Company could also be adversely affected by such factors as changes in foreign currency rates and weak economic and political conditions in each of the countries in which the Company sells its products.

s. Recently Issued Accounting Pronouncements

The Financial Accounting Standards Board (FASB) has adopted SFAS No. 151, Inventory Costs an Amendment of ARB No. 43, Chapter 4. The provisions of SFAS 151 are intended to eliminate narrow differences between the existing accounting standards of the FASB and the International Accounting Standards Board (IASB) related to inventory costs, in particular, the treatment of abnormal idle facility expense, freight, handling costs and spoilage. SFAS 151 requires that these costs be recognized as current period charges regardless of the extent to which they are considered abnormal. The provisions of SFAS 151 are effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The adoption of SFAS 151 did not have a significant impact on the Company s results of operations, financial position or cash flows.

During 2005, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets which eliminates the exception to the fair-value principle for exchanges of similar productive assets, which had been accounted for based on the book value of the asset surrendered with no gain recognition. Nonmonetary exchanges have to be accounted for at fair-value, recognizing any gain or loss, if the transactions meet the commercial-substance criterion and fair-value determinable. The Statement reduces the differences between U.S. and international accounting standards. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The Company adopted this Statement in the first quarter of fiscal 2006 and the pronouncement did not have a material impact on the Company s consolidated financial position, results of operations or cash flows.

During 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections (SFAS 154). SFAS 154 is a replacement of Accounting Principles Board No. 20, Accounting Changes and FASB Statement No. 3 Reporting Accounting Changes in Interim Financial Statement. SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application as the required method for reporting a change in accounting principle. SFAS 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. The reporting of a correction of an error by restating previously issued financial statements is also addressed by SFAS 154. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 31, 2005. The Company adopted this pronouncement in the first quarter of 2006.

In December 2004, the FASB issued FASB Staff Position No. FAS 109-1 (FSP FAS 109-1), Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities provided by the American Jobs Creation Act of 2004. FSP FAS 109-1 clarifies that the deduction will be treated as a special deduction as described in SFAS 109, Accounting for Income Taxes. As such, the special deduction has no effect on deferred tax assets and liabilities existing at the date of enactment. The impact of the deduction will be reported in the period in which the deduction is claimed. The incentive for U.S. qualified production activities included in the Act is effective as of December 21, 2004.

3. Intangible Assets

The Company s intangible assets at March 31, 2006 consisted entirely of goodwill which is not amortizable in accordance with SFAS No. 142. In applying SFAS No. 142, the Company performed the annual reassessment and impairment test in the fourth quarter of 2005 and determined that goodwill was not impaired. The goodwill is recorded at a cost of $3,720,743 reduced by accumulated amortization of $1,253,524 at March 31, 2006 and December 31, 2005, respectively.

The Company s amortizable intangible assets became fully amortized during 2005. The Company recorded amortization expense relating to identifiable intangible assets of $0 and $10,066 for the three months ending March 31, 2006 and 2005, respectively.

4. Inventories

Inventories consist of the following:

	March 31, 2006	December 31, 2005
Raw materials and components	$ 7,892,863	$ 7,008,791
Work in process	1,489,628	1,339,323
Finished goods	1,827,196	1,593,951
	$ 11,209,687	$ 9,942,065

The inventory balances are net of reserves for slow moving or obsolete inventory of approximately $1,270,000 and $1,138,000 as of March 31, 2006 and December 31, 2005, respectively.

5. Property, Plant and Equipment

Property, plant and equipment include the following:

	March 31, 2006	December 31 2005
Land	$ 343,500	$ 343,500
Buildings and improvements	4,699,981	4,699,981
Machinery and equipment	9,562,615	9,511,671
Office furniture and fixtures	2,276,370	2,212,273
Construction in process	33,184	39,155
	16,915,650	16,806,580
Less accumulated depreciation	11,696,875	11,426,647
Net property, plant and equipment	$ 5,218,775	$ 5,379,933

Depreciation expense amounted to $279,934 and $281,405 for the three months ending March 31, 2006 and 2005, respectively.

6. Debt

The Company is a party to a revolving credit facility with First National Bank of Omaha expiring August 28, 2006. The Company expects to renew the credit facility in the ordinary course of business. The credit facility provides for borrowings up to the lesser of $4.0 million or amounts determined by an asset based lending formula, as defined. Borrowings available under the credit facility amounted to $4.0 million at March 31, 2006. No amounts are currently outstanding. The Company would pay interest on outstanding amounts equal to the Prime Rate plus 0.25% (8.0% at March 31, 2006) and pays a fee of 0.125% on the unused portion. The credit facility contains certain restrictive covenants primarily related to maintaining certain earnings, as defined, and restrictions on acquisitions and dividends. All of the Company s personal property and stock in its subsidiaries secure this credit facility.

Long-term debt at March 31, 2006 consisted entirely of installment payments relating to the purchase of certain intangible assets. Future maturities of long-term debt for the remainder of fiscal 2006 and the remaining year in 2007 are $20,998 and $14,608, respectively.

7. Supplemental Cash Flow Information

Supplemental disclosures to the consolidated statements of cash flows are as follows:

	Three Months Ended March 31,	
	2006	2005

Interest paid	$	1,938	$	2,488
Income taxes paid	$	2,400	$	62,401
Income tax benefit related to stock option plans	$	180,397	$	
Share-based compensation expense related to liability classified awards	$	7,942	$	

8. Stockholder Rights Plan

On May 26, 2000, the Board of Directors of the Company adopted a Stockholder Rights Plan (the Rights Plan). Under terms of the Rights Plan, which expires June 9, 2010, the Company declared a distribution of one right for each outstanding share of common stock. The rights become exercisable only if a person or group (other than certain exempt persons, as defined) acquires 15 percent or more of Ballantyne common stock or announces a tender offer for 15 percent or more of Ballantyne s common stock. Under certain circumstances, the Rights Plan allows stockholders, other than the acquiring person or group, to purchase the Company s common stock at an exercise price of half the market price.

9. Postretirement Health Care

The Company sponsors a postretirement health care plan (the Plan) for certain current and former executives and their spouses. The Company s policy is to fund the cost of the Plan as expenses are incurred. The costs of the postretirement benefits are accrued over the employees service lives.

In accordance with SFAS No. 132, *Disclosures About Pensions and Other Postretirement Benefits*, the following table sets forth the components of the net period benefit cost for the three months ended March 31, 2006 and 2005:

	2006	2005
Service cost	$ 3,116	$ 3,051
Interest cost	6,083	6,196
Amortization of prior-service cost	6,718	6,718
Amortization of loss		934
Net periodic benefit cost	$ 15,917	$ 16,899

The Company expects to pay $6,045 under the plan in 2006. As of March 31, 2006, benefits of $348 have been paid.

In December 2003, the United States enacted into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act). The Act established a prescription drug benefit under Medicare, known as Medicare Part D and a federal subsidy to sponsors of retired healthcare benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. On May 19, 2004, the FASB issued Staff Position No. FAS-106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (FSP-106-2), which requires measures of the accumulated postretirement benefit obligation and net periodic postretirement benefit costs to reflect the effects of the Act in the first interim or annual period beginning after June 15, 2004. On January 21, 2005, final regulations under the Act were issued. The effects of the Act did not have a material impact on the consolidated financial statements of the Company.

10. Self-Insurance

The Company is self-insured up to certain stop loss limits for group health insurance. Accruals for claims incurred but not paid as of March 31, 2006 and December 31, 2005 are included in accrued group health insurance claims in the accompanying consolidated balance sheets. The Company s policy is to accrue the employee health benefit accruals based on historical information along with certain assumptions about future events.

11. Business Segment Information

The presentation of segment information reflects the manner in which management organizes segments for making operating decisions and assessing performance.

As of March 31, 2006, the Company s operations were conducted principally through three business segments: Theatre, Lighting and Restaurant. Theatre operations include the design, manufacture, assembly and sale of motion picture projectors, xenon lamphouses and power supplies, sound systems, film handling equipment and the sale of xenon lamps and lenses. The lighting segment operations include the design, manufacture, assembly and sale of follow spotlights, stationary searchlights and computer operated lighting systems for the motion picture production, television, live entertainment, theme parks and architectural industries. The restaurant segment includes the manufacture and sale of replacement parts and the sale of seasonings, marinades and barbeque sauces. The Company allocates resources to business segments and evaluates the performance of these segments based upon reported segment gross profit. However, certain key operations of a particular segment are tracked on the basis of operating profit. There are no significant intersegment sales. All intersegment transfers are recorded at historical cost.

Summary by Business Segments

	Three Months Ended March 31, 2006	2005
Net revenues		
Theatre	$ 11,132,206	$ 11,471,203
Lighting	1,120,424	829,364
Restaurant	180,708	211,302
Total net revenues	$ 12,433,338	$ 12,511,869
Gross profit		
Theatre	$ 2,932,970	$ 3,060,270
Lighting	318,643	254,994
Restaurant	79,354	79,327
Total gross profit	3,330,967	3,394,591
Selling and administrative expenses	(2,104,207)	(1,933,824)
Operating income	1,226,760	1,460,767
Net interest income	158,163	63,496
Other income (expense), net	18,880	(29,519)
Income before income taxes	$ 1,403,803	$ 1,494,744
Expenditures on capital equipment		
Theatre	$ 112,082	$ 78,297
Lighting	6,694	4,723
Total	$ 118,776	$ 83,020
Depreciation and amortization		
Theatre	$ 258,353	$ 275,759
Lighting	21,581	15,712
Total	$ 279,934	$ 291,471

	March 31, 2006	December 31, 2005
Identifiable assets		
Theatre	$ 44,139,302	$ 42,866,118
Lighting	4,362,660	3,382,738
Restaurant	754,263	687,071
Total	$ 49,256,225	$ 46,935,927

Summary by Geographical Area	**Three Months Ended March 31, 2006**	**2005**
Net revenue		
United States	$ 9,297,051	$ 8,600,561
Canada		