

BUTLER NATIONAL CORP  
Form 10-Q  
March 17, 2014

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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

For the quarterly period ended January 31, 2014

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

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

Commission File Number 0-1678

**BUTLER NATIONAL CORPORATION**

(Exact name of registrant as specified in its charter)

Kansas 41-0834293  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

19920 West 161st Street, Olathe, Kansas 66062  
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code: (913) 780-9595

Former name, former address and former fiscal year if changed since last report:  
Not Applicable

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 T No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files): Yes T No o

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes  No

The number of shares outstanding of the Registrant's Common Stock, \$0.01 par value, as of March 7, 2014 was 59,619,173 shares.

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

As of January 31, 2014 and April 30, 2013

(in thousands except per share data)

(unaudited)

	January 31, 2014	April 30, 2013
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash	\$5,071	\$5,148
Notes and accounts receivable	1,862	2,697
Income tax receivable	210	1,395
Inventories		
Raw materials	6,245	6,216
Work in process	2,134	1,048
Finished goods	151	240
Total inventory	8,530	7,504
Prepaid expenses and other current assets	767	829
Total current assets	16,440	17,573
<b>PROPERTY, PLANT AND EQUIPMENT:</b>		
Land and building	4,044	4,027
Aircraft	6,723	6,723
Machinery and equipment	3,494	3,714
Office furniture and fixtures	6,451	6,358
Leasehold improvements	4,060	4,060
	24,772	24,882
Accumulated depreciation	(11,404)	(9,435)
Total property, plant and equipment	13,368	15,447
<b>SUPPLEMENTAL TYPE CERTIFICATES (net of amortization of \$2,643 at January 31, 2014 and \$2,604 at April 30, 2013)</b>		
	1,976	2,014
<b>OTHER ASSETS:</b>		
Deferred tax asset	1,727	1,303
Other assets (net of accumulated amortization of \$2,191 at January 31, 2014 and \$1,213 at April 30, 2013)	7,604	7,523
Total other assets	9,331	8,826
Total Assets	\$41,115	\$43,860
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Promissory notes	\$1,744	\$1,377

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Current maturities of long-term debt and capital lease obligations	4,263	4,551
Accounts payable	1,251	1,509
Customer deposits	1,080	193
Gaming facility mandated payment	1,009	1,337
Compensation and compensated absences	989	1,045
Other current liabilities	256	119
Total current liabilities	10,592	10,131
LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS, NET OF CURRENT MATURITIES:		
Total liabilities	7,665	10,155
	18,257	20,286
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock, par value \$5: Authorized 50,000,000 shares, all classes Designated Classes A and B 200,000 shares \$1,000 Class A, 9.8 %, cumulative if earned liquidation and redemption value \$100, no shares issued and outstanding	-	-
\$1,000 Class B, 6 %, convertible cumulative, liquidation and redemption value \$1,000, no shares issued and outstanding	-	-
Common stock, par value \$.01: authorized 100,000,000 shares issued and outstanding 59,619,173 shares at January 31, 2014 and 59,619,173 shares at April 30, 2013	596	596
Capital contributed in excess of par	13,056	13,034
Treasury stock at cost, 600,000 shares	(732 )	(732 )
Retained Earnings	7,168	8,022
Total stockholders' equity Butler National Corporation	20,088	20,920
Noncontrolling Interest in BHCMC, LLC	2,770	2,654
Total stockholders' equity	22,858	23,574
Total Liabilities and Stockholders' Equity	\$41,115	\$43,860
The accompanying notes are an integral part of these financial statements		

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE THREE MONTHS ENDED JANUARY 31, 2014 AND 2013  
(in thousands, except per share data)  
(unaudited)

	THREE MONTHS ENDED January 31,	
	2014	2013
REVENUE:		
Professional Services	\$7,333	\$8,328
Aerospace Products	3,860	2,672
Total revenue	11,193	11,000
COSTS AND EXPENSES:		
Cost of Professional Services	4,498	5,304
Cost of Aerospace Products	2,843	2,492
Marketing and advertising	868	784
Employee benefits	571	586
Depreciation and amortization	870	848
General, administrative and other	1,525	1,505
Total costs and expenses	11,175	11,519
OPERATING INCOME (LOSS)	18	(519 )
OTHER INCOME (EXPENSE):		
Interest expense	(348 )	(417 )
Other income, net	2	-
Total other income (expense)	(346 )	(417 )
INCOME (LOSS) BEFORE INCOME TAXES	(328 )	(936 )
PROVISION (BENEFIT) FOR INCOME TAXES	(101 )	(200 )
NET INCOME (LOSS)	(227 )	(736 )
Net income attributable to noncontrolling interest in BHCMC, LLC	8	(19 )
NET INCOME (LOSS) ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION	\$(219 )	\$(755 )
BASIC EARNINGS PER COMMON SHARE	\$0.00	\$(0.01 )
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	59,019,173	57,542,914
DILUTED EARNINGS PER COMMON SHARE	\$(0.01 )	\$(0.01 )
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	59,019,173	57,542,914

The accompanying notes are an integral part of these financial statements



BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE NINE MONTHS ENDED JANUARY 31, 2014 AND 2013  
(in thousands, except per share data)  
(unaudited)

	NINE MONTHS ENDED January 31,	
	2014	2013
REVENUE:		
Professional Services	\$23,934	\$27,305
Aerospace Products	9,819	10,700
Total revenue	33,753	38,005
COSTS AND EXPENSES:		
Cost of Professional Services	14,068	15,811
Cost of Aerospace Products	7,787	8,593
Marketing and advertising	3,185	2,901
Employee benefits	1,651	1,590
Depreciation and amortization	2,630	2,304
General, administrative and other	4,470	5,341
Total costs and expenses	33,791	36,540
OPERATING INCOME (LOSS)	(38 )	1,465
OTHER INCOME (EXPENSE):		
Interest expense	(1,100 )	(1,095 )
Other income, net	42	10
Total other income (expense)	(1,058 )	(1,085 )
INCOME (LOSS) BEFORE INCOME TAXES	(1,096 )	380
PROVISION (BENEFIT) FOR INCOME TAXES	(359 )	8
NET INCOME (LOSS)	(737 )	372
Net income attributable to noncontrolling interest in BHCMC, LLC	(116 )	(745 )
NET INCOME (LOSS) ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION	\$(853 )	\$(373 )
BASIC EARNINGS PER COMMON SHARE	\$0.00	\$(0.01 )
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	59,019,173	57,537,995
DILUTED EARNINGS PER COMMON SHARE	\$(0.01 )	\$(0.01 )
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	59,019,173	57,537,995

The accompanying notes are an integral part of these financial statements





BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 FOR THE NINE MONTHS ENDED JANUARY 31, 2014 AND 2013

(in thousands)

(unaudited)

	NINE MONTHS ENDED	
	January 31,	
	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income (loss)	\$(737 )	\$372
Adjustments to reconcile cash flows from operating activities		
Depreciation and amortization	3,255	2,417
Stock issued for services	22	91
Stock options issued to employees and directors	-	107
Gain and loss on disposal of other assets	(36 )	-
Changes in assets and liabilities		
Accounts receivable	974	1,621
Income tax receivable	1,185	-
Inventories	(1,116)	(6 )
Prepaid expenses and other current assets	62	(1,878)
Accounts payable	(258 )	539
Customer deposits	887	(624 )
Accrued liabilities	(56 )	(199 )
Gaming facility mandated payment	(328 )	777
Other liabilities	136	84
Deferred tax asset	(424 )	-
Other assets	12	-
Cash flows from operating activities	3,578	3,301
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	(174 )	(6,724)
Cash flows from investing activities	(174 )	(6,724)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Borrowings of promissory notes, net	-	3,416
Borrowings of promissory notes, long-term debt and capital lease obligations	(3,848)	(2,361)
Repayments of promissory notes, long-term debt and capital lease obligations	(3,481)	1,430
Cash flows from financing activities	(3,481)	1,430
<b>NET DECREASE IN CASH</b>	<b>(77 )</b>	<b>(1,993)</b>
CASH, beginning of period	5,148	7,431
CASH, end of period	\$5,071	\$5,438

## SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

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Interest paid	\$1,102	\$1,095
Income taxes paid	\$-	\$783

NON CASH OPERATING ACTIVITY

Non cash stock issued for services	\$22	\$91
Non cash stock options issued to employees and directors	\$-	\$107
Capitalized lease intangible assets	\$1,070	\$1,182
Capitalized lease obligation	\$1,070	\$1,182

The accompanying notes are an integral part of these financial statements

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BUTLER NATIONAL CORPORATION AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

(unaudited)

1. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Therefore, these financial statements should be read in conjunction with the annual report on Form 10-K for the fiscal year ended April 30, 2013. In our opinion, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three and nine months ended January 31, 2014 are not indicative of the results of operations that may be expected for the fiscal year ended April 30, 2014.

Certain reclassifications within the condensed financial statement captions have been made to maintain consistency in presentation between years. Financial amounts are in thousands of dollars except per share amounts.

2. Net Income (Loss) Per Share: The Company follows ASC 260 that requires the reporting of both basic and diluted earnings (loss) per share. Basic earnings (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. In accordance with ASC 260, any anti-dilutive effects on net earnings (loss) per share are excluded. Potential common shares as of January 31, 2014 are 66,281,237.

3. Research and Development: We invested in research and development activities. The amount invested in the nine months ended January 31, 2014 and 2013 was \$1,569 and \$1,268 respectively.

4. Borrowings: At January 31, 2014, the Company was utilizing three lines of credit totaling \$4.0 million. The unused line at January 31, 2014 was \$2.3 million. During the current year these funds were primarily used for the purchase of inventory and aircraft modification STC development for the modifications and avionics operations.

Our \$1.0 million line of credit has been extended to August 2014. Our \$2.5 million line of credit matures April 2015. Our \$0.5 million line of credit matures June 2015. The lines of credit are collateralized by the first and second positions on all assets of the Company.

At January 31, 2014, there were several notes collateralized by aircraft security agreements totaling \$1,370. These notes were used for the purchase and modifications of these collateralized aircraft and Kings Avionics, Inc.

There are three notes at a bank totaling \$1,493 for real estate located in Olathe, Kansas and Tempe, Arizona. The due date for these notes is March 2019 and August 2019.

One note totaling \$323 remain for real estate purchased in November 2007 and June 2009 in Dodge City, Kansas.

BHCMC entered into an obligation with Konami Gaming Inc. effective August 1, 2012 in the amount of \$1,733. The purchase of the gaming system was installed at Boot Hill Casino in mid-August and has a current balance of \$518.

The Kansas Lottery acquired additional gaming machines. BHCMC, as manager under the management contract with the State of Kansas, was required to remit payment for the gaming equipment. The balance of this financed payable is \$1,145.

We are not in default of any of our notes as of January 31, 2014.

We believe that our current banks will provide the necessary capital for our business operations. However, we continue to maintain contact with other banks that have an interest in funding our working capital needs to continue our growth in operations in 2014 and beyond.

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5. Leases: BHCMC, LLC ("BHCMC") as tenant entered into a lease dated May 1, 2011, and amended via an addendum dated January 1, 2012 (collectively, the "Lease"), with BHC Investment Company, L.C. ("BHCI") as landlord for a total obligation of \$7,423. BHCI provided funds to BHCMC for the purchase of certain intangible items and gaming items related to the Boot Hill Casino. Commencing on January 1, 2012, BHCMC is obligated to make a minimum payment to BHCI of \$177 per month until September 30, 2017. The remaining balance on the obligation is \$4,981.

On August 24, 2012 BHCMC and BHCI entered into a second lease ("Second Lease") of \$2,500 for tenant improvements related to expansion of the Boot Hill Casino. Commencing on November 1, 2012, BHCMC is obligated to make a minimum payment to BHCI of approximately \$55 per month until November 30, 2017. The remaining obligation is \$2,007.

6. Other Assets: Our other asset account includes assets of \$5,500 related to the Kansas Expanded Lottery Act Management Contract privilege fee, \$2,252 of gaming equipment we were required to pay for ownership by the State of Kansas Lottery, and JET autopilot intellectual property of \$1,417. BHCMC expects the \$5,500 privilege fee to have a value over the remaining life of the Management Contract with the State of Kansas which will end in December 2024. There is no assurance of the Management Contract renewal. The Managers Certificate asset for use of gaming equipment is being amortized over a period of three years based on the estimated useful life of gaming equipment. The JET intellectual property is being amortized over a period of 15 years.

7. Stockholders' Equity: On May 8, 2012, the Company issued 238,750 shares of Company common stock to Reign Strategy & Investment Group, LLC ("RSIG"). The market value was \$91 at date of issue. These shares were issued in consideration for RSIG's marketing and consulting services related to increasing public awareness and shareholder interest in the Company.

The issuance of stock by the Company to RSIG is exempt from registration pursuant to Rule 506 of Regulation D promulgated under the Securities Act of 1933, as amended. RSIG has represented to the Company and the Company believes that RSIG is an "accredited investor" as defined in Rule 501(a) of Regulation D.

8. Stock Options: At January 31, 2014 we had 7,262,064 outstanding stock options that were issued on December 31, 2010 all of which expire on December 31, 2015.

The exercise price for the incentive stock options is \$0.49. The Board of Directors approved the issuance of incentive stock options on December 31, 2010 with the goals of increasing shareholder value, expanding the number of managers participating in the program, and increasing the percentage of compensation tied to share price performance.

The incentive stock options are allocated in three groups with two conditions for vesting. The first condition is stock price and the second condition is time. There are 2,420,688 options at \$0.49 that may be exercised if and when the share price reaches \$0.92, and 2,420,688 options at \$0.49 that may be exercised if and when the share price reaches \$1.41, and 2,420,688 options at \$0.49 that may be exercised on or after December 31, 2013 if and when the share price reaches \$1.90

9. Subsequent Events: BHCMC, LLC and BHC Development, LC filed a lawsuit in the United States District Court for the District of Kansas on June 21, 2012 against Bally Gaming, Inc. doing business as Bally Technologies for negligent misrepresentations, among other claims related to the performance of computer software systems. On March 7, 2014 a jury verdict in favor of BHCMC, LLC and BHC Development against Bally was entered for approximately \$1.4 million. The jury rejected the Bally alleged counter claim of \$441 and awarded no damages to Bally. Bally has a right to appeal the verdict.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THROUGHOUT THIS ITEM 2 ALL NON TABULAR FINANCIAL RESULTS ARE PRESENTED IN THOUSANDS OF U.S. DOLLARS EXCEPT WHERE MILLIONS OF DOLLARS IS INDICATED.

Forward Looking Statements

Statements made in this report, filed with the Securities and Exchange Commission, communications to stockholders, press releases, and oral statements made by representatives of the Company that are not historical in nature, or that state the Company or management intentions, hopes, beliefs, expectations or predictions of the future, may constitute "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements can often be identified by the use of forward-looking terminology, such as "could," "should," "will," "intended," "continue," "believe," "may," "expect," "hope," "anticipate," "goal," "forecast," "plan," "guidance" or "estimate" or the negative of these words, variations thereof or similar expressions. Forward-looking statements are not guarantees of future performance or results. They involve risks, uncertainties, and assumptions. It is important to note that any such performance and actual results, financial condition or business, could differ materially from those expressed in such forward-looking statements. These risks, uncertainties and other factors include those set forth in Item 1A (Risk Factors) of this Quarterly Report on Form 10-Q and reference to the Cautionary Statements filed by us as Exhibit 99 to the Annual Report on Form 10-K including the following factors:

- the impact of general economic trends on the Company's business;
- the deferral or termination of programs or contracts for convenience by customers;
- market acceptance of the Company's Aerospace Products and or other planned products or product enhancements;
- increased fuel and energy costs and the downward pressure on demand for our aircraft business;
- the ability to gain and maintain regulatory approval of existing products and services and receive regulatory approval of new businesses and products;
- the actions of regulatory, legislative, executive or judicial decisions of the federal, state or local level with regard to our business and the impact of any such actions;
- failure to retain/recruit key personnel;
- the availability of government funding;
- any delays in receiving components from third party suppliers;
- the competitive environment;
- the bankruptcy or insolvency of one or more key customers;
- new product offerings from competitors;
- protection of intellectual property rights;
- the ability to service the international market;
- acts of terrorism and war and other uncontrollable events;
- joint ventures and other arrangements;
- low priced penny-stock regulations;
- general governance features;
- United States and other country defense spending cuts;
- our estimated effective income tax rates; estimated tax benefits; and merits of our tax position
- potential future acquisitions; and
- other factors disclosed from time to time in the Company's filings with the Securities and Exchange Commission.

Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the Cautionary Statements and Risk Factors, filed as Exhibit 99 and Item 1A. Risk Factors to the Company's Annual

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Report on Form 10-K for the fiscal year ended April 30, 2013 are incorporated herein by reference. Other unforeseen factors not identified herein could also have such an effect. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes in future operating results, financial condition or business over time.

### Management Overview

Management is focused on increasing long-term shareholder value from increased cash generation, earnings growth, and prudently managing capital expenditures. We plan to do this by continuing to drive increased revenue from product and service innovations, strategic acquisitions, and targeted marketing programs.

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Our revenue is primarily derived from two very different business segments; Aerospace Products and Professional Services. These segments operate through various Butler National Corporation subsidiaries and affiliates listed in the Company's fiscal year 2013 annual report on Form 10K.

Aerospace Products derives its revenue by designing system integration, engineering, manufacturing, installing, servicing, and repairing products for classic and current production aircraft. These products include JET autopilot service and repairs, Avcon provisions and system integration for special mission equipment installations, Kings Avionics equipment sales and installation, and Butler National electronic controls and safety equipment manufacture and sales. Aerospace customers range in size from owners and operators of small single engine airplanes to owners and operators of large commercial and military aircraft. Aerospace Products are sold to and serviced for customers located in many countries of the world.

Aerospace is the legacy part of the Butler National business. Organized over 50 years ago, this business is based upon design engineering and installation innovations to enhance and support products related to airplanes and ground support equipment. These new products included: in the 1960's, aircraft electronic load sharing and system switching equipment, a number of airplane electronic navigation instruments, radios and transponders; in the 1970's, ground based VOR navigation equipment sold worldwide and GPS equipment as we know it today in civilian use; in the 1980's, special mission modifications to business jets for aerial surveillance and conversion of passenger configurations to cargo; in the 1990's, classic aviation support of aging airplanes with enhanced protection of electrical systems through transient suppression devices (TSD), control electronics for military weapon systems and improved aerodynamic control products (Avcon Fins) allowing stability at higher gross weights for additional special mission applications; in the 2000's, improved accuracy of the airspeed and altimeter systems to allow less vertical separation between flying airplanes (RVSM) and acquisition of the JET autopilot product line to support and replace aged electronic equipment in the classic fleet of Learjet airplanes; and in the 2010's, the acquisition of Kings Avionics to provide additional classic airplane support by retrofit of avionics from the past 40 years to modern state of the art equipment for sale worldwide using FAA supplemental type certification to make the installations (STC) acceptable to foreign governments for installation abroad.

Aerospace continues to be a focus for new product design and development. Our recent approval is noise suppression for Learjet 20 series aircraft. We expect this segment will continue to grow in the future. To address the three to five year business cycles related to the Aerospace industry, in the 1990's, we began providing Professional Services to markets outside the Aerospace industry.

Professional Services derives its revenue from (a) professional management services in the gaming industry through Butler National Service Corporation ("BNSC") and BHCMC, LLC ("BHCMC"), (b) licensed architectural services to the business community through BCS Design ("BCS"), and (c) monitoring services to owners and operators of intelligence gathering systems through Butler National Services, Inc. ("BNSI").

Professional Services grew from the experiences gained from the BNSI monitoring products and services of the 1980's including SCADA systems and products including digital voice technology for the telephone industry and nuclear plant and civil defense warning systems. BNSI sold these Professional Services and products to utilities and municipalities resulting in relatively stable revenue streams. The defense warning products were sold in the 1980's to a third party leaving only the BNSI service business in Florida (on May 1, 2013 we sold our waste water monitoring business (Butler National Services, Inc.) to Beadle Enterprises, LLC.

In the early 1990's, management determined that more revenue stable business units were needed to sustain the Company. Members of the Board of Directors had contacts with several American Indian tribes and other members of the Board were associated with gaming operators in Las Vegas. After enactment of the 1988 Indian Gaming Regulatory Act (IGRA) we reached out to various Indian tribes with land in the area to explore the opportunities for operations under IGRA. This resulted in the "Stables" an Indian owned casino on Modoc Indian land opened in

September 1998 developed and managed by BNSC. The Stables Management Agreement has been available on the website maintained by the National Indian Gaming Commission ("NIGC"). The Stables Management Agreement was subsequently amended by various amendments dated April 30, 2003 (the "First Amendment"), November 30, 2006 (the "Second Amendment"), October 19, 2009 (the "Third Amendment") and September 22, 2011 (the "Fourth Amendment"). The result of the First Amendment, Second Amendment, Third Amendment and Fourth Amendment is to provide that twenty (20%) of net profits from The Stables are distributed to BNSC, to end per the joint venture agreement the participation of the Miami Indian tribe from the business and to extend the duration of the Stables Management Agreement through September 30, 2018. BCS Design assisted with the design, construction and continued refurbishment of the Stables.

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From this experience with IGRA and the success of the Indian gaming industry, we determined that the IGRA model may be applicable for state owned gaming. We spent Butler National Corporation innovation, legal and market development funds to design and encourage the use of an Indian owned gaming model in the State of Kansas. From these efforts, Kansas enacted the Kansas Expanded Lottery Act (KELA) in 2007 allowing four state owned casinos to be developed in Kansas. In 2007, BNSC made application to manage a state owned casino. In 2008, BNSC was awarded a fifteen year term to manage the Boot Hill Casino in Dodge City, Kansas pursuant to a Lottery Gaming Facility Management Contract (the "Boot Hill Casino Management Contract"). The Boot Hill Casino Management Contract was amended on December 29, 2009 (the "First Amendment to the Boot Hill Casino Management Contract") to bring the definition of "Fiscal Year" in line with the fiscal year of BNSC (May 1 to April 30). BHCMC was organized to be the manager of the Boot Hill Casino in Dodge City, Kansas. The casino opened in December 2009. BCS Design assisted with the design, construction and continued refurbishment of Boot Hill Casino.

The Phase II expansion of Boot Hill Casino began in early 2012 and was completed in January 2013. The unfinished gaming floor space built during Phase I construction and tenant improvements was funded by tenant improvement leases, gaming machine leases, and casino earnings, with minimum exposure to Butler National Corporation. The Phase II expansion included the interior finish of 15,000 square feet of casino shell and 216 additional gaming machines. Part of the expansion included a breezeway connecting the Boot Hill Casino and the Dodge City special events center (United Wireless Arena). In late January 2013 the snack bar was reopened with additional seating and space as the "Cowboy Cafe." BCS Design assisted with the design, construction and continued refurbishment of Boot Hill Casino.

#### Results Overview

The nine months ending January 31, 2014 revenue decreased 11% to \$33.8 million compared to \$38.0 million in the nine months ending January 31, 2013. In the nine months ending January 31, 2014 the professional services revenue was \$23.9 million compared to \$27.3 million in the nine months ending January 31, 2013, a decrease of 12%. In the nine months ending January 31, 2014 the Aerospace Products revenue was \$9.8 million compared to \$10.7 million in the nine months ending January 31, 2013, a decrease of 8%.

The nine months ending January 31, 2014 net income decreased to a loss of \$853 compared to a loss of \$373 in the nine months ending January 31, 2013. We continue focusing on our margin expansion initiatives, including implementation of efficiencies in our operational processes and controlling general and administrative expenses. The nine months ending January 31, 2014, operating income (loss) was \$(38), a decrease of 103% from our operating income of \$1,465 in the nine months ending January 31, 2013.

#### RESULTS OF OPERATIONS

##### NINE MONTHS ENDING JANUARY 31, 2014 COMPARED TO NINE MONTHS ENDING JANUARY 31, 2013

	Nine Months Ended Jan. 31, 2014		Nine Months Ended Jan. 31, 2013		Percent Change 2013-2014
	Revenue	Percent of Total Revenue	Revenue	Percent of Total Revenue	
(dollars in thousands)					
Revenue:					
Professional Services	\$23,934	71 %	\$27,305	72 %	(12 %)
Aerospace Products	9,819	29 %	10,700	28 %	(8 %)
Total revenue	33,753	100 %	38,005	100 %	(11 %)

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								%
Costs and expenses:								)
Cost of Professional Services	14,068	42	%	15,811	42	%	(11	%
								)
Cost of Aerospace Products	7,787	23	%	8,593	23	%	(9	%
Marketing and advertising	3,185	9	%	2,901	8	%	10	%
Employee benefits	1,651	5	%	1,590	4	%	4	%
Depreciation and amortization	2,630	8	%	2,304	6	%	14	%
								)
General, administrative and other	4,470	13	%	5,341	14	%	(16	%
								)
Total costs and expenses	33,791	100	%	36,540	97	%	(8	%
								)
Operating income (loss)	\$(38 )	0	%	\$1,465	3	%	(103	%
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Revenue:

Revenue decreased 11% to \$33.8 million in the nine months ended January 31, 2014, compared to \$38.0 million in the nine months ended January 31, 2013.

Professional Services derives its revenue from professional management services in the gaming industry through BNSC and BHCMC, licensed architectural services to the business community through BCS Design. Revenue from Professional Services decreased 12% to \$23.9 million in the nine months ended January 31, 2014 from \$27.3 million in the nine months ended January 31, 2013.

Aerospace Products derives its revenue by system integration, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft. Aerospace Products revenue decreased 8% for the nine months to \$9.8 million at January 31, 2014 compared to \$10.7 million at January 31, 2013.

Costs and expenses:

Costs and expenses related to Professional Services and Aerospace Products include the cost of engineering, labor, materials, equipment utilization, control systems, security and occupancy.

Costs and expenses decreased 8% in the nine months ended January 31, 2014 to \$33.8 million compared to \$36.5 million in the nine months ended January 31, 2013. Costs and expenses were 100% of total revenue in the nine months ended January 31, 2014, as compared to 97% of total revenue in the nine months ended January 31, 2013. The increased costs and expenses as a percent of total revenue in the nine months ended January 31, 2014 were primarily driven by a decrease in revenue. Total costs and expenses were reduced by approximately \$2.7 million.

Marketing and advertising expenses as a percent of total revenue was 9% in the nine months ended January 31, 2014, as compared to 8% in the nine months ended January 31, 2013. These expenses increased 10% to \$3.2 million in the nine months ended January 31, 2014, from \$2.9 million in the nine months ended January 31, 2013. Marketing and advertising expenses include advertising, sales and marketing labor, gaming development costs, and casino and product promotions.

Employee benefits expenses as a percent of total revenue was 5% in the nine months ended January 31, 2014, compared to 4% in the nine months ended January 31, 2013. These expenses increased 4% to \$1.7 million in the nine months ended January 31, 2014, from \$1.6 million in the nine months ended January 31, 2013. These expenses include the employers' share of all federal, state and local taxes, paid time off for vacation, holidays and illness, employee health and life insurance programs and employer matching contributions to retirement plans. The increased expenses are related to increases in insurance cost.

Depreciation and amortization expenses as a percent of total revenue was 8% in the nine months ended January 31, 2014, compared to 6% in the nine months ended January 31, 2013. These expenses increased 14% to \$2.6 million in the nine months ended January 31, 2014, from \$2.3 million in the nine months ended January 31, 2013. These expenses include depreciation related to owned assets being depreciated over various useful lives and amortization of intangible items including the Kansas privilege fee related to the Boot Hill Casino being expensed over the term of the gaming contract with the State of Kansas. Phase II expansion to Boot Hill Casino was formally completed in early January 2013 and we began depreciation on \$4.9 million of assets with various useful lives. BHCMC, LLC depreciation and amortization expense for the nine months ended January 31, 2014 was \$1.2 million compared to \$848 at January 31, 2013.

General, administrative and other expenses as a percent of total revenue was 13% in the nine months ended January 31, 2014, compared to 14% in the nine months ended January 31, 2013. These expenses decreased 16% to \$4.5 million in the nine months ended January 31, 2014, from \$5.3 million in the nine months ended January 31, 2013. The

decrease reflects our cost reduction plan to align overall expenses with the current level of revenue in the Aerospace business segment. The plan includes reductions in staffing levels and reductions of top-level management compensation.

Other income (expense):

Interest expense and other income were \$1.1 million in the nine months ended January 31, 2014 compared with interest expense and other income of \$1.1 million in the nine months ended January 31, 2013. Interest expense was stable from the nine months ended January 31, 2013 to the nine months ended January 31, 2014. Interest of \$885 was related to obligations of BHCMC, LLC. A gain on the sale of assets was recorded for Butler National Services, Inc. in the amount of \$36.

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Operations by Segment

We have two operating segments, Professional Services and Aerospace Products. The Professional Services segment includes revenue contributions and expenditures associated with monitoring services for SCADA systems owned by others, professional architectural services and casino management services. Aerospace Products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft.

The following table presents a summary of our operating segment information for the nine months ended January 31, 2014 and January 31, 2013:

(dollars in thousands)	Nine Months Ended Jan. 31, 2014			Nine Months Ended Jan. 31, 2013			Percent Change 2013-2014	
		Percent of Revenue			Percent of Revenue			
Professional Services Revenue								)
Boot Hill Casino	\$22,212	93 %		\$24,054	88 %		(8	%
Management/Professional Services Revenue	1,722	7 %		3,251	12 %		(47	%
	23,934	100 %		27,305	100 %		(12	%
Costs of Professional Services Expenses	14,068	59 %		15,811	58 %		(11	%
Total costs and expenses	23,068	97 %		25,053	92 %		(8	%
Professional Services operating income before noncontrolling interest in BHCMC, LLC	\$866	3 %		\$2,252	8 %		(62	%

(dollars in thousands)	Nine Months Ended Jan. 31, 2014			Nine Months Ended Jan. 31, 2013			Percent Change 2013-2014	
		Percent of Revenue			Percent of Revenue			
Aerospace Products Revenue	\$9,819	100 %		\$10,700	100 %		(8	%
Costs of Aerospace Products Expenses	7,787	79 %		8,593	80 %		(9	%
	2,936	30 %		2,894	27 %		1	%
Total costs and expenses	10,723	109 %		11,487	107 %		(7	%
Aerospace Products operating income (loss)	\$(904)	(9 %)		\$(787)	(7 %)		15	%

Professional Services

Revenue from Professional Services decreased 12% to \$23.9 million for the nine months ended January 31, 2014, compared to \$27.3 million for the nine months ended January 31, 2013.

In the nine months ended January 31, 2014 Boot Hill Casino and Resort received gross receipts for the State of Kansas of \$29.9 million compared to \$31.8 million for the nine months ended January 31, 2013. Mandated fees, taxes and distributions reduced gross receipts by \$9.9 million resulting in gaming revenue of \$20.0 million for the nine months ended January 31, 2014 compared to a reduction to gross receipts of \$10.2 million for the nine months ended January 31, 2013 a decrease of 3%.

The remaining management and Professional Services revenue include professional management services in the gaming industry, licensed architectural services, food, beverage, and retail from Boot Hill Casino. Management and Professional Services revenue decreased to \$1.7 million for the nine months ended January 31, 2014 compared to \$3.3 million for the nine months ended January 31, 2013 a decrease of 47%.

Costs decreased 11% in the nine months ended January 31, 2014 to \$14.1 million compared to \$15.8 million in the nine months ended January 31, 2013. Costs were 59% of segment total revenue in the nine months ended January 31, 2014, as compared to 58% of segment total revenue in the nine months ended January 31, 2013. The decrease in direct costs were a result of reductions of electronic gaming machines.

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Expenses decreased 3% in the nine months ended January 31, 2014 to \$9.0 million compared to \$9.2 million in the nine months ended January 31, 2013. Expenses were 38% of segment total revenue in the nine months ended January 31, 2014, as compared to 34% of segment total revenue in the nine months ended January 31, 2013.

**Aerospace Products**

Revenue decreased 8% to \$9.8 million in the nine months ended January 31, 2014 compared to \$10.7 million in the nine months ended January 31, 2013. This decrease is attributable to reduced revenue of \$1.1 million in the modification business. In an effort to offset decreased domestic military spending, we continue to invest in the development of STCs. These STCs are state of the art avionics, noise suppression and special mission products. We are aggressively marketing both domestically and internationally.

Costs decreased by 9% in the nine months ended January 31, 2014 to \$7.8 million compared to \$8.6 million for the nine months ended January 31, 2013. Costs were 79% of segment total revenue in the nine months ended January 31, 2014, as compared to 80% of segment total revenue in the nine months ended January 31, 2013.

Expenses increased 1% in the nine months ended January 31, 2014 at \$2.9 million compared to \$2.9 million in the nine months ended January 31, 2013. Expenses were 30% of segment total revenue in the nine months ended January 31, 2014, as compared to 27% of segment total revenue in the nine months ended January 31, 2013.

**Employees**

Other than persons employed by our gaming subsidiaries there were 81 full time and 3 part time employee on January 31, 2014 compared to 98 full time and 2 part time employees on January 31, 2013. As of March 7, 2014, staffing is 81 full time and 3 part time employees. Our staffing at Boot Hill Casino & Resort on January 31, 2014 was 197 full time and 37 part time employees. At March 7, 2014 there are 200 full time employees and 41 part time employees. None of the employees are subject to any collective bargaining agreements.

**THIRD QUARTER FISCAL 2014 COMPARED TO THIRD QUARTER FISCAL 2013**

	Three Months Ended Jan. 31, 2014		Three Months Ended Jan. 31, 2013		Percent Change 2013-2014	
	Revenue	Percent of Total Revenue	Revenue	Percent of Total Revenue	Revenue	Percent of Total Revenue
(dollars in thousands)						
Revenue:						
Professional Services	\$7,333	66 %	\$8,328	76 %	(12 %)	
Aerospace Products	3,860	34 %	2,672	24 %	44 %	
Total revenue	11,193	100 %	11,000	100 %	2 %	
Costs and expenses:						
Cost of Professional Services	4,498	40 %	5,304	48 %	(15 %)	
Cost of Aerospace Products	2,843	25 %	2,492	23 %	14 %	
Marketing and advertising	868	8 %	784	7 %	11 %	
Employee benefits	571	5 %	586	5 %	(3 %)	
Depreciation and amortization	870	8 %	848	8 %	3 %	
General, administrative and other	1,525	14 %	1,505	14 %	1 %	

Total costs and expenses	11,175	100	%	11,519	105	%	(3	)	%
Operating income (loss)	\$18	0	%	\$(519	)	(5	%	103	%

Revenue:

Revenue increased 2% to \$11.2 million in the three months ended January 31, 2014, compared to \$11.0 million in the three months ended January 31, 2013.

Professional Services derives its revenue from professional management services in the gaming industry through BNSC and BHCMC, licensed architectural services to the business community through BCS Design. Revenue from Professional Services decreased 12% for the three months ended to \$7.3 million at January 31, 2014, compared to \$8.3 million at January 31, 2013.

Aerospace Products derives its revenue by system integration, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft. Aerospace Products revenue increased 44% for the three months to \$3.9 million at January 31, 2014 compared to \$2.7 million at January 31, 2013.

Costs and expenses:

Costs and expenses related to Professional Services and Aerospace Products include the cost of engineering, labor, materials, equipment utilization, control systems, security and occupancy.

Costs and expenses decreased 3% in the three months ended January 31, 2014 to \$11.2 million compared to \$11.5 million in the three months ended January 31, 2013. Costs and expenses were 100% of total revenue in the three months ended January 31, 2014, as compared to 105% of total revenue in the three months ended January 31, 2013. The decreased costs and expenses as a percent of total revenue in the three months ended January 31, 2014 were primarily driven by an increase in total revenue.

Marketing and advertising expenses as a percent of total revenue was 8% in the three months ended January 31, 2014, as compared to 7% in the three months ended January 31, 2013. These expenses were \$868 in the three months ended January 31, 2014, from \$784 in the three months ended January 31, 2013. Marketing and advertising expenses include advertising, sales and marketing labor, gaming development costs, and casino and product promotions.

Employee benefits expenses as a percent of total revenue was 5% in the three months ended January 31, 2014, compared to 5% in the three months ended January 31, 2013. These expenses were \$571 in the three months ended January 31, 2014, from \$586 in the three months ended January 31, 2013. These expenses include the employers' share of all federal, state and local taxes, paid time off for vacation, holidays and illness, employee health and life insurance programs and employer matching contributions to retirement plans.

Depreciation and amortization expenses as a percent of total revenue was 8% in the three months ended January 31, 2014, compared to 8% in the three months ended January 31, 2013. These expenses were \$870 in the three months ended January 31, 2014, from \$848 in the three months ended January 31, 2013. These expenses include depreciation related to owned assets being depreciated over various useful lives and amortization of intangible items including the Kansas privilege fee related to the Boot Hill Casino being expensed over the term of the gaming contract with the State of Kansas. Phase II expansion to Boot Hill Casino was formally completed in early January 2013 and we began depreciation on \$4.9 million of assets with various useful lives. BHCMC, LLC depreciation and amortization expense for the three months ended January 31, 2014 was \$401 compared to \$361 at January 31, 2013.

General, administrative and other expenses as a percent of total revenue was 14% in the three months ended January 31, 2014, compared to 14% in the three months ended January 31, 2013. These expenses were \$1.5 million in the three months ended January 31, 2014, from \$1.5 million in the three months ended January 31, 2013.

Other income (expense):

Interest expense and other income was \$346 in the three months ended January 31, 2014 compared with interest expense and other income of \$417 in the three months ended January 31, 2013. Interest expense decreased 17% from the three months ended January 31, 2013 to the three months ended January 31, 2014. Interest of \$274 was related to obligations of BHCMC, LLC.

Operations by Segment

We have two operating segments, Professional Services and Aerospace Products. The Professional Services segment includes revenue contributions and expenditures associated with monitoring services for SCADA systems owned by

others, professional architectural services and casino management services. Aerospace Products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft.

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The following table presents a summary of our operating segment information for the three months ended January 31, 2014 and January 31, 2013:

(dollars in thousands)	Three Months Ended Jan. 31, 2014			Three Months Ended Jan. 31, 2013			Percent Change 2013-2014
	Revenue	Percent of Revenue		Revenue	Percent of Revenue		
Professional Services Revenue							)
Boot Hill Casino	\$6,882	94 %		\$7,470	90 %	(8 %)	)
Management/Professional Services Revenue	451	6 %		858	10 %	(47 %)	)
	7,333	100 %		8,328	100 %	(12 %)	)
Costs of Professional Services	4,498	61 %		5,304	64 %	(15 %)	)
Expenses	2,729	37 %		2,778	33 %	(2 %)	)
Total costs and expenses	7,227	98 %		8,082	97 %	(11 %)	)
Professional Services operating income (loss) before noncontrolling interest in BHCMC, LLC	\$106	2 %		\$246	3 %	(57 %)	)

(dollars in thousands)	Three Months Ended Jan. 31, 2014			Three Months Ended Jan. 31, 2013			Percent Change 2013-2014
	Revenue	Percent of Revenue		Revenue	Percent of Revenue		
Aerospace Products Revenue	\$3,860	100 %		\$2,672	100 %	44 %	)
Costs of Aerospace Products	2,843	74 %		2,492	93 %	14 %	)
Expenses	1,105	29 %		945	35 %	17 %	)
Total costs and expenses	3,948	103 %		3,437	128 %	15 %	)
Aerospace Products operating income (loss)	\$(88 )	(3 %)		\$(765 )	(28 %)	88 %	)

Professional Services

Revenue from Professional Services decreased 12% to \$7.3 million for the three months ended January 31, 2014, compared to \$8.3 million for the three months ended January 31, 2013.

In the three months ended January 31, 2014 Boot Hill Casino and Resort received gross receipts for the State of Kansas of \$9.4 million compared to \$10.0 million for the three months ended January 31, 2013. Mandated fees, taxes and distributions reduced gross receipts by \$3.2 million resulting in gaming revenue of \$6.2 million for the three months ended January 31, 2014 compared to a reduction to gross receipts of \$3.3 million for the three months ended

January 31, 2013 a decrease of 3%.

The remaining management and Professional Services revenue include professional management services in the gaming industry, licensed architectural services, food, beverage, and retail from Boot Hill Casino. Management and Professional Services revenue decreased to \$451 for the three months ended January 31, 2014 compared to \$858 for the three months ended January 31, 2013 a decrease of 47%.

Costs decreased 15% in the three months ended January 31, 2014 to \$4.5 million compared to \$5.3 million in the three months ended January 31, 2013. Costs were 61% of segment total revenue in the three months ended January 31, 2014, as compared to 64% of segment total revenue in the three months ended January 31, 2013. The decrease in direct costs was a result of reductions of electronic gaming machines.

Expenses decreased 2% in the three months ended January 31, 2014 to \$2,729 compared to \$2,778 in the three months ended January 31, 2013. Expenses were 37% of segment total revenue in the three months ended January 31, 2014, as compared to 33% of segment total revenue in the three months ended January 31, 2013.

### Aerospace Products

Revenue increased 44% to \$3.9 million in the three months ended January 31, 2014 compared to \$2.7 million in the three months ended January 31, 2013. This increase is attributable to increased revenue of \$1.1 million in the modification business. In an effort to offset decreased domestic military spending, we continue to invest in the development of several STCs. These STCs are state of the art avionics, noise suppression and special mission products. We are aggressively marketing both domestically and internationally.

Costs increased by 14% in the three months ended January 31, 2014 to \$2.8 million compared to \$2.5 million for the three months ended January 31, 2013. Costs were 74% of segment total revenue in the three months ended January 31, 2014, as compared to 93% of segment total revenue in the three months ended January 31, 2013.

Expenses increased 17% in the three months ended January 31, 2014 at \$1,105 compared to \$945 in the three months ended January 31, 2013. Expenses were 29% of segment total revenue in the three months ended January 31, 2014, as compared to 35% of segment total revenue in the three months ended January 31, 2013..

### Liquidity and Capital Resources

We believe that our current banks will provide the necessary capital for our business operations. However, we continue to maintain contact with other banks that have an interest in funding our working capital needs to continue our growth in operations in fiscal 2014 and beyond.

The ownership structure of BHCMC, LLC is now:

Membership Interest	Members of Board of Managers	Equity Ownership	Income (Loss) Sharing	
Class A	3	20	%	40 %
Class B	4	80	%	60 %

BHCMC, LLC, rents the casino building under the terms of a 25 year lease from BHC Development L.C. "BHCD". Butler National Corporation, its management, or subsidiaries have no ownership interest in BHCI or BHCD.

The terms of the agreement between the Kansas Lottery and BNSC/BHCMC require the completion of an addition to the Boot Hill Casino. The Phase II development of an adjacent hotel and community owned special events center was funded by a third party, is completed, and open to the public. The Phase II expansion of Boot Hill Casino began in early 2012 and was completed in January 2013. Phase II expansion of the unfinished gaming floor space built during Phase I construction and tenant improvements was funded by tenant improvement leases, gaming machine leases, and casino earnings, with minimum exposure to Butler National Corporation. The Phase II expansion included the interior finish of 15,000 square feet of casino shell and 216 additional gaming machines. Part of the expansion included a breezeway connecting the Boot Hill Casino and the Dodge City special events center (United Wireless Arena). In late January 2013 the snack bar was reopened with additional seating and space as the "Cowboy Cafe."

### Analysis and Discussion of Cash Flow

During the nine months ended January 31, 2014 our cash position decreased by \$77. We had a net loss of \$737. Cash flows from operating activities provided \$3,578. Non-cash activities consisting of depreciation and amortization contributed \$3,255 and stock options issued to employees and directors contributed \$22. Customer deposits increased our cash position by \$887, in addition to a net change income tax receivable of \$1,185 and prepaid expenses of \$62. A decrease in accounts receivable of \$974, increases in inventory of \$1,116 and decreases in accounts payable and

accrued expenses of \$314 decreased our cash position. We had a gain on the sale of select assets in the amount of \$36.

Cash used in investing activities was \$174. We invested \$17 for property improvements in Dodge City and invested approximated \$157 for equipment at Boot Hill Casino and Resort.

Cash used in financing activities was \$3,481. We reduced our debt by \$3,848 and increased our line of credit by \$367. The increase borrowings on the line of credit were a result of the development of the Learjet 20 series stage 3 noise suppression system and Learjet under wing hard points.

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Critical Accounting Policies and Estimates:

We believe that there are several accounting policies that are critical to understanding our historical and future performance, as these policies affect the reported amount of revenue and other significant areas involving management judgments and estimates. These significant accounting policies relate to revenue recognition, the use of estimates, long-lived assets, and Supplemental Type Certificates. These policies and our procedures related to these policies are described in detail below and under specific areas within this "Management Discussion and Analysis of Financial Condition and Results of Operations."

**Revenue Recognition:** Generally, we perform aircraft modifications under fixed-price contracts. Revenue from fixed-price contracts are recognized on the percentage-of-completion method, measured by the direct labor and material costs incurred compared to total estimated direct labor costs. Each quarter our management reviews the progress and performance of our significant contracts. Based on this analysis, any adjustment to sales, cost of sales and/or profit is recognized as necessary in the period they are earned. Changes in estimates of contract sales, cost of sales and profits are recognized using a cumulative catch-up, which is recognized in the current period of the cumulative effect of the change on current or prior periods. Revenue for off-the-shelf items and aircraft sales is recognized on the date of sale.

Revenue from product sales are recognized when shipped. Payment is due for these products within 30 days of the invoice date after shipment. Revenue for Gaming Management, and other Corporate/Professional Services are recognized as the service is rendered and invoiced. Payments for these service invoices are usually received within 30 days.

In regard to warranties and returns, our products are special order and are not suitable for return. Our products are unique upon installation and tested prior to their release to the customer and acceptance by the customer. In the rare event of a warranty claim, the claim is processed through the normal course of business and may include additional charges to the customer. In our opinion any future warranty work would not be material to the financial statements.

Gaming revenue is the gross gaming win as reported by the Kansas Lottery casino reporting systems, less the mandated payments by and for the State of Kansas. Electronic games-slots and table games revenue is the aggregate of gaming wins and losses. Liabilities are recognized for chips and "ticket-in, ticket-out" coupons in the customers' possession, and for accruals related to anticipated payout of progressive jackpots. Progressive gaming machines, which contain base jackpots that increase at a progressive rate based on the number of coins played, are deducted from revenue as the amount of jackpots increase. Food, beverage, and other revenue is recorded when the service is rendered.

**Use of Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Future events and their effects cannot be determined with certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results could differ from those estimates, and any such differences may be material to our financial statements.

**Long-lived Assets:** The Company accounts for its long-lived assets in accordance with ASC Topic 360-10, formerly SFAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets." ASC Topic 360-10 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the historical cost carrying value of an asset may no longer be appropriate. The Company assesses recoverability of the carrying value of an asset by estimating the future net cash flows expected to result from the asset, including eventual disposition. If the future net cash flows are less than the carrying value of the asset, an impairment loss is recorded

equal to the difference between the asset's carrying value and fair value or disposable value.

Supplemental Type Certificates: Supplemental Type Certificates (STCs) are authorizations granted by the Federal Aviation Administration (FAA) for specific modification of a certain aircraft. The STC authorizes us to perform modifications, installations, and assemblies on applicable customer-owned aircraft. Costs incurred to obtain STCs are capitalized and subsequently amortized against revenue being generated from aircraft modifications associated with the STC. The costs are expensed as services are rendered on each aircraft through costs of sales using the units of production method. The legal life of an STC is indefinite. We believe we have enough future sales to fully amortize our STC development costs.

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### Changing Prices and Inflation

We have experienced upward pressure from inflation in fiscal year 2014. From fiscal year 2013 to fiscal year 2014 a majority of the increases we experienced were in material costs. This additional cost may not be transferable to our customers resulting in lower income in the future. We anticipate fuel costs and possibly interest rates to rise in fiscal 2015 and 2016.

### Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

### Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Please see Item 7(a) of our Form 10-K for the period ended April 30, 2013, which such Item is incorporated herein by reference.

### Item 4. CONTROLS AND PROCEDURES

We maintain a set of disclosure controls and procedures designed to ensure that information required to be disclosed in our filings under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission rules and forms. Our principal executive and financial officers have evaluated our disclosure controls and procedures as of the end of the period covered by this report on Form 10-K and have determined that such disclosure controls and procedures are effective, based on criteria in Internal Control-Integrated Framework, issued by COSO.

Evaluation of disclosure controls and procedures: Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosures.

In connection with the preparation of this Form 10-Q, our Chief Executive Officer and our Chief Financial Officer conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of January 31, 2014. Based on that evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of January 31, 2014.

### Internal Control Over Financial Reporting

Changes in Internal Control Over Financial Reporting: In our opinion there were no material changes in the Company internal controls over financial reporting during the quarter covered in this report that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

### Limitations on Controls

Our management, including the Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision making can be faulty and that breakdowns can occur

because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

PART II. - OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS.

BHCMC, LLC and BHC Development, LC filed a lawsuit in the United States District Court for the District of Kansas on June 21, 2012 against Bally Gaming, Inc. doing business as Bally Technologies for negligent misrepresentations, among other claims related to the performance of computer software systems. On March 7, 2014 a jury verdict in favor of BHCMC, LLC and BHC Development against Bally was entered for approximately \$1,423,542. The jury rejected the Bally alleged counter claim of \$441,000 and awarded no damages to Bally. Bally has a right to appeal the verdict.

Item 1A. RISK FACTORS.

There are no material changes to the risk factors disclosed under Item 1A of our Form 10-K for the fiscal year ended April 30, 2013.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES.

None.

Item 4. MINE SAFETY DISCLOSURES.

None.

Item 5. OTHER INFORMATION.

On March 12, 2013 the Company amended its bylaws to include Section 1.11, which now requires stockholder proposals (including proposals relating to the nomination of a director) to be provided in writing not less than 120 days before the first anniversary of the mailing date of the notice of the preceding year's stockholder annual meeting. The full bylaws of the Company are attached hereto as Exhibit 3.2 and incorporated herein by reference. The addition of Section 1.11 to the bylaws does not change the date upon which stockholder proposals must be received by the Company's Secretary (such date remains May 3, 2014, as previously identified in the Company's definitive proxy statement for the 2013 annual meeting of stockholders). New Section 1.11 of the Company's bylaws also requires that a stockholder proposal must contain the information required by the Securities Exchange Act of 1934 for any nominee to the board of directors. The submission to the Company must also include a brief description of the business proposed to be brought for the stockholder meeting, the reasons for conducting such business, a description of any material interest the person making the proposal may have in such business, and such information as to permit the Company to confirm the ownership of the Company's common stock held by the person making the proposal.

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Item 6. EXHIBITS

3.1 Articles of Incorporation, as amended and restated are incorporated by reference to Exhibit 3.1 of our Form DEF 14A filed on December 26, 2001.

3.2 Bylaws, as amended, are approved by the Board of Directors on March 12, 2013.

31.1 Certificate of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a).

31.2 Certificate of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a).

32.1 Certifications of Chief Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certifications of Chief Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

99 Cautionary Statements for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995, are incorporated by reference to Exhibit 99 of the Form 10-K for the fiscal year ended April 30, 2013.

101 The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended January 31, 2014, formatted in XBRL (Extensible Business Reporting Language) includes: (i) Condensed Consolidated Balance Sheets as of January 31, 2014 and April 30, 2013, (ii) Condensed Consolidated Statements of Operations for the three months ended January 31, 2014 and nine months ended January 31, 2014, (iii) Condensed Consolidated Statements of Cash Flows for the nine months ended January 31, 2014 and 2013, and (iv) the Notes to Consolidated Financial Statements, with detail tagging. In accordance with Regulation S-T, the XBRL-formatted interactive data files that comprise this Exhibit 101 shall be deemed "furnished" and not "filed."

SIGNATURES

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

BUTLER NATIONAL CORPORATION  
(Registrant)

March 17, 2014 /s/ Clark D. Stewart  
Date Clark D. Stewart  
(President and Chief Executive Officer)

March 17, 2014 /s/ Craig D. Stewart  
Date Craig D. Stewart  
(Chief Financial Officer)

Exhibit Index

Exhibit Number	Description of Exhibit
10.1	Lease between Butler National Service Corporation and BHC Development, L.C., dated April 30, 2009
10.2	Legal Description Lot 1 in a future replat of Mariah Center
10.3	Legal Description Lot 2 in a future replat of Mariah Center
3.1	Articles of Incorporation, as amended and restated are incorporated by reference to Exhibit 3.1 of our Form DEF 14A filed on December 26, 2001.
3.2	Bylaws, as amended, are incorporated by reference to Exhibit A of this Form 10Q filed on March 12, 2013.
31.1	Certificate of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a).
31.2	Certificate of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a).
32.1	Certifications of Chief Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certifications of Chief Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99	Cautionary Statements for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995, are incorporated by reference to Exhibit 99 of the Form 10-K for the fiscal year ended April 30, 2013.
101	The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended January 31, 2014, formatted in XBRL (Extensible Business Reporting Language) includes: (i) Condensed Consolidated Balance Sheets as of January 31, 2014 and April 30, 2013, (ii) Condensed Consolidated Statements of Operations for the three months ended January 31, 2014 and 2013, (iii) Condensed Consolidated Statements of Cash Flows for the nine months ended January 31, 2014 and 2013, and (iv) the Notes to Consolidated Financial Statements, with detail tagging. In accordance with Regulation S-T, the XBRL-formatted interactive data files that comprise this Exhibit 101 shall be deemed "furnished" and not "filed."