

AEROSONIC CORP /DE/  
Form 10-Q  
August 26, 2005

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

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

For the quarterly period ended July 29, 2005

**OR**

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**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 1-11750**

**AEROSONIC CORPORATION**

**(Exact name of registrant as specified in its charter)**

**Delaware 74-1668471**

**(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)**

**1212 North Hercules Avenue**

**Clearwater, Florida 33765**

**(Address of principal executive offices and Zip Code)**

**Registrant's telephone number, including area code: (727) 461-3000**

**Not Applicable**

**(Former name, former address and former fiscal year, if changed since last report)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes  No

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

As of August 25, 2005, the issuer had 3,921,019 shares of Common Stock outstanding, net of treasury shares.

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## PART I FINANCIAL INFORMATION

### Forward-Looking Statements

**THIS DOCUMENT INCLUDES CERTAIN FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. THESE FORWARD-LOOKING STATEMENTS INCLUDE, BUT ARE NOT LIMITED TO OUR PLANS, OBJECTIVES, EXPECTATIONS AND INTENTIONS AND OTHER STATEMENTS CONTAINED IN THIS REPORT THAT ARE NOT HISTORICAL FACTS AS WELL AS STATEMENTS IDENTIFIED BY WORDS SUCH AS EXPECTS, ANTICIPATES, INTENDS, PLANS, BELIEVES, SEEKS, ESTIMATES OF SIMILAR MEANING. THESE STATEMENTS ARE BASED ON OUR CURRENT BELIEFS OR EXPECTATIONS AND ARE INHERENTLY SUBJECT TO SIGNIFICANT UNCERTAINTIES AND CHANGES IN CIRCUMSTANCES, MANY OF WHICH ARE BEYOND OUR CONTROL. ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THESE EXPECTATIONS DUE TO CHANGES IN GLOBAL POLITICAL, ECONOMIC, BUSINESS, COMPETITIVE, MARKET AND REGULATORY FACTORS.**

### Significant Events

On July 13, 2005, all parties to the securities class action lawsuit in the Federal District Court of the Middle District of Florida (the **Federal Class Action** ) filed a Stipulation of Settlement (the **Stipulation** ) to settle the Federal Class Action. The Stipulation provides for a payment by or on behalf of the defendants to the plaintiffs of approximately \$5.35 million. Of this amount, the Company is obligated to pay \$800,000, which has been accrued in the accompanying consolidated financial statements as of July 29, 2005 and January 31, 2005. The balance of the settlement is expected to be paid by Zurich American Insurance Company on behalf of the Company and the individual defendants under the Company's directors' and officers' insurance policy, and by PricewaterhouseCoopers LLP. On August 9, 2005, the court preliminarily approved the settlement and set a fairness hearing on November 18, 2005 to consider final approval of the settlement. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

On July 11, 2005, the plaintiffs of a Derivative Complaint filed by Matilda Franzitta (the **Franzitta Suit** ) voluntarily dismissed their claims against William Parker, a former director of the Company. On July 25, 2005, all parties filed a Stipulation of Settlement to settle the Franzitta Suit (the **Franzitta Stipulation** ). The settlement provides the Company appoint a new independent director to its board and grant standing authority to the Company's Audit Committee to investigate any matters it deems appropriate. The settlement also provides for a payment of up to \$75,000 in attorney's fees and costs to plaintiff's counsel, none of which is required to be paid by the Company. On August 16, 2005, the court preliminarily approved the settlement and set a final fairness hearing on November 21, 2005. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

Note 9 of Item 1 of Part I of this report include discussions of: (i) a securities class action lawsuit filed against the Company, PricewaterhouseCoopers LLP, the Company's former independent accountant, and four former employees of the Company, two of whom were directors, and (ii) a derivative suit filed against certain present and former directors, officers, and employees of the Company as well as PricewaterhouseCoopers LLP, the Company's former independent accountant.

**Table of Contents****Item 1 Financial Statements**

**AEROSONIC CORPORATION AND SUBSIDIARY**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

|   | <b>July 29, 2005</b><br><b>(unaudited)</b> | <b>January 31, 2005</b> |
|---|--|-------------------------|
|   | <b>ASSETS</b>                              |                         |
| Current assets:   |  |                         |
| Cash and cash equivalents                                       | \$ 2,759,000                               | \$ 840,000              |
| Receivables, net of allowance for doubtful accounts of \$14,000 |  |                         |
|   | 5,513,000                                  | 3,708,000               |
| Income taxes receivable   | 292,000                                    | 899,000                 |
| Costs less estimated losses in excess of billings               | 732,000                                    | 1,942,000               |
| Inventories   | 5,852,000                                  | 5,483,000               |
| Prepaid expenses  | 332,000                                    | 198,000                 |
| Deferred income taxes   | 1,236,000                                  | 1,236,000               |
| Total current assets  | 16,716,000                                 | 14,306,000              |
| Property, plant and equipment, net                              | 3,698,000                                  | 3,842,000               |
| Deferred income taxes   | 123,000                                    | 123,000                 |

|  |               |               |
|--|---------------|---------------|
| Capitalized software costs and other assets, net | 176,000       | 192,000       |
| Total assets                                     | \$ 20,713,000 | \$ 18,463,000 |

### LIABILITIES AND STOCKHOLDERS EQUITY

|  |            |            |
|--|------------|------------|
| Current liabilities:   |            |            |
| Long-term debt and notes payable due within one year   | \$ 230,000 | \$ 243,000 |
| Accounts payable, trade  | 2,550,000  | 1,600,000  |
| Compensation and benefits  | 933,000    | 938,000    |
| Income taxes payable   | 476,000    | -          |
| Accrued expenses and other liabilities   | 2,400,000  | 2,404,000  |
| Total current liabilities  | 6,589,000  | 5,185,000  |
| Long-term debt and notes payable due after one year  | 2,679,000  | 2,794,000  |
| Other long-term liabilities  | 30,000     | -          |
| Total liabilities  | 9,298,000  | 7,979,000  |
| Commitments and contingencies (Note 9)   |            |            |
| Stockholders equity:   |            |            |
| Common stock \$0.40 par value: authorized 8,000,000; shares issued 3,986,262; shares outstanding 3,921,019 | 1,595,000  | 1,595,000  |



|   |               |               |
|---|---------------|---------------|
| Additional paid-in capital                  |               |               |
|   | 4,559,000     | 4,559,000     |
| Retained earnings                           |               |               |
|   | 5,957,000     | 5,026,000     |
| Less treasury stock: 65,243 shares, at cost |               |               |
|   | (696,000)     | (696,000)     |
| Total stockholders' equity                  |               |               |
|   | 11,415,000    | 10,484,000    |
| Total liabilities and stockholders' equity  |               |               |
|   | \$ 20,713,000 | \$ 18,463,000 |

The accompanying notes are an integral part of these condensed consolidated financial statements

**Table of Contents****AEROSONIC CORPORATION AND SUBSIDIARY****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (unaudited)**

|   | <b>Three Months Ended</b> |                      | <b>Six Months Ended</b> |                      |
|---|---------------------------|----------------------|-------------------------|----------------------|
|   | <b>July 29, 2005</b>      | <b>July 30, 2004</b> | <b>July 29, 2005</b>    | <b>July 30, 2004</b> |
| Revenue, net                                    |                           |                      |                         |                      |
|   | \$ 8,977,000              | \$ 7,937,000         | \$ 18,052,000           | \$ 15,033,000        |
| Cost of revenue                                 |                           |                      |                         |                      |
|   | 5,966,000                 | 5,220,000            | 12,516,000              | 10,308,000           |
| Gross profit                                    |                           |                      |                         |                      |
|   | 3,011,000                 | 2,717,000            | 5,536,000               | 4,725,000            |
| Selling, general and<br>administrative expenses | 2,175,000                 | 2,273,000            | 3,988,000               | 4,052,000            |
| Operating income                                |                           |                      |                         |                      |
|   | 836,000                   | 444,000              | 1,548,000               | 673,000              |
| Other income (expense):                         |                           |                      |                         |                      |
| Interest expense, net                           |                           |                      |                         |                      |
|   | (30,000)                  | (46,000)             | (73,000)                | (52,000)             |
| Miscellaneous income<br>(expense)               |                           |                      |                         |                      |
|   | (15,000)                  | 1,058,000            | 40,000                  | 1,179,000            |
|   | (45,000)                  | 1,012,000            | (33,000)                | 1,127,000            |
| Income before income taxes                      |                           |                      |                         |                      |
|   | 791,000                   | 1,456,000            | 1,515,000               | 1,800,000            |
| Income tax expense                              |                           |                      |                         |                      |
|   | (309,000)                 | (553,000)            | (584,000)               | (688,000)            |
| Net income                                      |                           |                      |                         |                      |
|   | \$ 482,000                | \$ 903,000           | \$ 931,000              | \$ 1,112,000         |

Average shares outstanding

Basic

|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
|  | 3,921,019 | 3,921,019 | 3,921,019 | 3,921,019 |
|--|-----------|-----------|-----------|-----------|

Diluted

|  |           |           |           |           |
|--|-----------|-----------|-----------|-----------|
|  | 3,921,019 | 3,921,019 | 3,921,019 | 3,921,019 |
|--|-----------|-----------|-----------|-----------|

Earnings per share

Basic

|  |         |         |         |         |
|--|---------|---------|---------|---------|
|  | \$ 0.12 | \$ 0.23 | \$ 0.24 | \$ 0.28 |
|--|---------|---------|---------|---------|

Diluted

|  |         |         |         |         |
|--|---------|---------|---------|---------|
|  | \$ 0.12 | \$ 0.23 | \$ 0.24 | \$ 0.28 |
|--|---------|---------|---------|---------|

The accompanying notes are an integral part of these condensed consolidated financial statements

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**AEROSONIC CORPORATION AND SUBSIDIARY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**

|   | <b>Six Months Ended</b> |                      |
|---|-------------------------|----------------------|
|   | <b>July 29, 2005</b>    | <b>July 30, 2004</b> |
| <b>Cash flow from operating activities:</b>   |                         |                      |
| Net income  |                         |                      |
|   | \$ 931,000              | \$ 1,112,000         |
| Adjustments to reconcile net income to net cash provided by/<br>(used in) operating activities: |                         |                      |
| Allowance for doubtful accounts   |                         |                      |
|   | -                       | (140,000)            |
| Depreciation  |                         |                      |
|   | 335,000                 | 303,000              |
| Amortization  |                         |                      |
|   | 13,000                  | 27,000               |
| Loss on disposal of property  |                         |                      |
|   | 8,000                   | -                    |
| Changes in assets and liabilities:  |                         |                      |
| Receivables   |                         |                      |
|   | (1,805,000)             | (819,000)            |
| Income taxes receivable and payable   |                         |                      |
|   | 1,083,000               | 1,077,000            |
| Costs less estimated losses in excess of billings   |                         |                      |
|   | 1,210,000               | (541,000)            |
| Inventories   |                         |                      |
|   | (369,000)               | (21,000)             |
| Prepaid expenses  |                         |                      |
|   | (134,000)               | 2,000                |
| Capitalized software costs and other assets   |                         |                      |
|   | 3,000                   | (73,000)             |
| Accounts payable, trade   |                         |                      |
|   | 950,000                 | (1,283,000)          |

|  |              |            |
|--|--------------|------------|
| Compensation and benefits                              |              |            |
|  | (5,000)      | 232,000    |
| Accrued expenses and other liabilities                 |              |            |
|  | 26,000       | (723,000)  |
| Net cash provided by/ (used in) operating activities   |              |            |
|  | 2,246,000    | (847,000)  |
| <b>Cash flow from investing activities:</b>            |              |            |
| Proceeds from the sale of property                     |              |            |
|  | 2,000        | -          |
| Capital expenditures                                   |              |            |
|  | (201,000)    | (148,000)  |
| Net cash used in investing activities                  |              |            |
|  | (199,000)    | (148,000)  |
| <b>Cash flow from financing activities:</b>            |              |            |
| Proceeds/ (payments) from revolving credit facilities  |              |            |
|  | -            | (400,000)  |
| Proceeds from issuance of long-term debt               |              |            |
|  | -            | 621,000    |
| Principal payments on long-term debt and notes payable |              |            |
|  | (128,000)    | (70,000)   |
| Net cash provided by/ (used in) financing activities   |              |            |
|  | (128,000)    | 151,000    |
| Net increase/ (decrease) in cash and cash equivalents  |              |            |
|  | 1,919,000    | (844,000)  |
| Cash and cash equivalents at beginning of period       |              |            |
|  | 840,000      | 1,276,000  |
| Cash and cash equivalents at end of period             |              |            |
|  | \$ 2,759,000 | \$ 432,000 |

Supplemental disclosure of cash flow information:

Cash paid during the period for:

Interest

|  |    |        |    |        |
|--|----|--------|----|--------|
|  | \$ | 92,000 | \$ | 94,000 |
|--|----|--------|----|--------|

Income taxes

|  |    |   |    |         |
|--|----|---|----|---------|
|  | \$ | - | \$ | 300,000 |
|--|----|---|----|---------|

Non cash investing and financing activities:

Acquisition of property through issuance of note payable

|  |    |   |    |         |
|--|----|---|----|---------|
|  | \$ | - | \$ | 211,000 |
|--|----|---|----|---------|

The accompanying notes are an integral part of these condensed consolidated financial statements

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**AEROSONIC CORPORATION AND SUBSIDIARY**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

**Note 1 Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements of Aerosonic Corporation (the **Company**) for the three months and the six months ended July 29, 2005 and July 30, 2004 have been prepared in accordance with generally accepted accounting principles for interim financial reporting and with the instructions to Form 10-Q and in Regulation S-X of the U.S. Securities and Exchange Commission ( **SEC** ). Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The July 29, 2005 consolidated balance sheet has been derived from the audited consolidated financial statements, but does not include all of the disclosures required by accounting principles generally accepted in the United States of America. The financial statements are prepared on a consistent basis (including normal recurring adjustments) and should be read in conjunction with the consolidated financial statements and related notes contained in the Annual Report on Form 10-K for the fiscal year ended January 31, 2005 (the **2005 Form 10-K**) that the Company filed with the SEC on April 18, 2005. Operating results for the three months and six months ended July 29, 2005 are not necessarily indicative of the results that may be expected for the year ending January 31, 2006.

**Note 2 Business**

The Company is principally engaged in one business segment which is the manufacture and service of aircraft instruments. The Company consists of three operating divisions in three locations. The divisions are: the Clearwater, Florida Instrument Division ( **Clearwater Instruments** ), the Aerosonic Wichita, Kansas Division ( **Kansas Instruments** ) and Avionics Specialties, Inc., a Virginia corporation wholly owned by the Company ( **Avionics** ).

Clearwater Instruments primarily manufactures altimeters, airspeed indicators, rate of climb indicators, microprocessor controlled air data test sets, and a variety of other flight instrumentation. Kansas Instruments is the source inspection location for our Wichita customers and is the primary location for Clearwater Instruments repair business. Avionics maintains three major product lines: (1) angle of attack stall warning systems; (2) integrated multifunction probes, which are integrated air data sensors; and (3) other aircraft sensors and monitoring systems.

During the three months ended July 29, 2005, sales to Lockheed Martin Corporation ( **Lockheed** ) represented approximately 12% of total revenues and sales to The Boeing Company represented approximately 10% of total revenues. During the three months ended July 30, 2004, sales to Lockheed Martin Corporation represented approximately 14% of total revenues and sales to Mid-Continent Instrument Company Inc. represented approximately 10% of total revenues. During the six months ended July 29, 2005 and July 30, 2004, sales to Lockheed represented approximately 18% and 17% of total revenues, respectively.

The Company has a January 31 fiscal year end. Accordingly, all references in this quarterly report on Form 10-Q to the second quarter mean the second quarter ended on the last Friday of July in the referenced fiscal year. For example, references to the second quarter of fiscal year 2006 mean the second quarter ended July 29, 2005.

**Note 3 Inventories**

Inventories are stated at the lower of cost (using a method that approximates the first-in, first-out method) or net realizable value. Cost is determined using a method that approximates the first-in, first-out method. Provisions are made for any inventory deemed excess or obsolete. Management employs certain methods to estimate the value of work in process inventories for financial reporting purposes. At fiscal year end, these estimates are affected by the nature of the operation at which the items are located and the time at which a physical inventory is conducted, and are subject to judgment. This practice was employed for the fiscal year ended January 31, 2005. For interim reporting periods, the Company utilizes monthly work in process inventory reports to estimate the value of such inventories.



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**Inventories at July 29, 2005 and January 31, 2005 consisted of the following:**

|  | <b>July 29, 2005</b> | <b>January 31, 2005</b> |
|--|----------------------|-------------------------|
|  | (unaudited)          |                         |
| Raw materials                                  |                      |                         |
|  | \$ 3,831,000         | \$ 3,475,000            |
| Work in process                                |                      |                         |
|  | 2,364,000            | 2,276,000               |
| Finished goods                                 |                      |                         |
|  | 100,000              | 133,000                 |
| Reserve for obsolete and slow moving inventory |                      |                         |
|  | (443,000)            | (401,000)               |
|  | \$ 5,852,000         | \$ 5,483,000            |

**Note 4 Joint Strike Fighter Development Program**

During fiscal 2003, the Company secured a long-term fixed-price contract for the development of instrumentation for the Joint Strike Fighter ( **JSF** ) program. Costs and estimated losses to date on this contract as of July 29, 2005 and January 31, 2005 are as follows:

|                        | <b>July 29, 2005</b> | <b>January 31, 2005</b> |
|------------------------|----------------------|-------------------------|
|                        | (unaudited)          |                         |
| Costs incurred to date |                      |                         |
|                        | \$ 13,742,000        | \$ 11,493,000           |
| Estimated losses       |                      |                         |
|                        | (1,442,000)          | (201,000)               |

|   |              |              |
|---|--------------|--------------|
|   | 12,300,000   | 11,292,000   |
| Less billings to date                             |              |              |
|   | (11,568,000) | (9,350,000)  |
| Costs less estimated losses in excess of billings |              |              |
|   | \$ 732,000   | \$ 1,942,000 |

During the quarter ended April 29, 2005, the Company developed a solution for a significant design element that it expects will reduce program costs. The Company believed that the reduction in costs could be recognized during the quarter ended July 29, 2005 after testing procedures were conducted prior to the solution being formally accepted as a design change by the project customer. The Company had planned to conduct these testing procedures in June 2005, but the testing facility at which the tests were to be conducted suffered a catastrophic failure shortly before the testing was scheduled to begin. As a result, testing of this solution has been delayed until the third quarter of fiscal year 2006. Consequently, the Company has not yet recognized any of the potential cost savings associated with this potential design improvement.

In addition to the delays caused by the unavailability of testing facilities and the incurrence of engineering and manufacturing costs to improve the producibility and the reliability of the probe design, the Company has recognized a loss of approximately \$184,000 to provide for expected future costs during the remainder of the program to complete the engineering design and production of the probes.

As a result of the foregoing, the estimated costs of the project increased by approximately \$738,000 and, as a result, estimated total program costs exceed estimated program revenues by approximately \$1,442,000. The Company has recognized the increase in estimated project costs of \$738,000 in its financial statements during the quarter ended July 29, 2005.

The JSF program is a customer-funded product development program that is presently expected to generate total project revenues of approximately \$16,336,000. As of July 29, 2005, based on project progress, the Company has recognized revenues of approximately \$12,300,000 for the JSF project. The estimate for this program changes with each technological breakthrough and setback and the Company will continue to adjust its estimate to reflect the most current view of the program's costs. The revenues and costs recorded in each quarter reflect the Company's best estimate of the program's expected profitability or loss at that point in time.



The JSF program represents a significant investment in the Company's future product development capabilities. While Company management is expending considerable effort to control costs and complete the development process on schedule, the key benefit to the program is the substantial revenue that the Company will earn if it is awarded the production contract for the JSF that is expected to follow the conclusion of the development program.

#### Note 5 Accrued Expenses

Accrued expenses as of July 29, 2005 and January 31, 2005 were approximately \$2,400,000 and \$2,404,000, respectively. A substantial portion of these expenses are related to amounts owed to subcontractors who participate in the Company's product development programs, as shown below:

|                                     | July 29, 2005<br>(unaudited) | January 31,<br>2005        |
|-------------------------------------|------------------------------|----------------------------|
| Product development programs        | \$<br>981,000                | \$<br>886,000              |
| Shareholder litigation (See Note 9) | 800,000                      | 800,000                    |
| Other accrued expenses              | 619,000<br>\$<br>2,400,000   | 718,000<br>\$<br>2,404,000 |

#### Note 6 Long Term Debt and Notes Payable

The Company's credit facilities are with Wachovia Bank, N.A. ( **Wachovia** ). The facilities total approximately \$5.7 million, and include a 15 year term loan of approximately \$3.0 million that is collateralized by the Company's real estate in Clearwater, Florida, a revolving credit facility of approximately \$2.5 million, and a seven year equipment loan of approximately \$0.2 million. All of the Company's other assets (i.e., other than the Clearwater real estate) are subject to liens collateralizing all three of the loans from Wachovia. This includes all assets of Avionics Specialties, Inc., the Company's wholly owned subsidiary.

Long term debt and notes payable at July 29, 2005 and January 31, 2005 consisted of the following:

|   | <b>July 29, 2005</b> | <b>January 31, 2005</b> |
|---|----------------------|-------------------------|
|   | (unaudited)          |                         |
| Mortgage note payable Wachovia                          | \$ 2,733,000         | \$ 2,833,000            |
| Equipment note payable Wachovia                         | 176,000              | 191,000                 |
| Capitalized leases                                      | -                    | 13,000                  |
|   | 2,909,000            | 3,037,000               |
| Less current maturity                                   | (230,000)            | (243,000)               |
| Long-term debt and notes payable, less current maturity | \$ 2,679,000         | \$ 2,794,000            |

### **Covenants**

The Company's long-term debt agreements with Wachovia contain certain financial and other restrictive covenants, including the requirement to maintain: (i) at all times, a ratio of total liabilities to tangible net worth that does not exceed 1.30 to 1.00; and (ii) at the end of each fiscal quarter, a cash flow coverage ratio (with regard to the debt service) of at least 1.25 to 1.00. As of July 29, 2005, the Company was in compliance with these financial covenants.

The Wachovia loan agreement subjects the Company to a number of additional covenants that, among other things, require the Company to obtain consent from the lender prior to making a material change of management, guarantee or otherwise become responsible for obligations of any other person or entity or assuming or becoming liable for any debt, contingent or direct, in excess of \$100,000.

The Company's ability to maintain sufficient liquidity and compliance with covenants in fiscal year 2006 and beyond is highly dependent upon achieving expected operating results. Failure to achieve expected operating results and compliance with covenants could have a material adverse effect on the Company's liquidity and operations in fiscal year 2006 and beyond, and could require implementation of further measures, including deferring planned capital expenditures, reducing discretionary spending, and/or, if necessary, selling assets.



**Note 7 Accounting for Stock-Based Compensation**

At July 29, 2005, the Company had a stock incentive plan (the "Plan"), which authorizes the issuance of options to purchase common stock. The Company has adopted the disclosure-only provisions of FAS 123, Accounting for Stock-Based Compensation, as amended by FAS 148, Accounting for Stock Based Compensation-Transition and Disclosure, an amendment of FASB Statement No. 123, but accounts for the plan under the recognition and measurement principles of Accounting Principles Board Opinion No. 25 and related interpretations.

No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. If the Company had elected to recognize compensation expense for stock options based on the fair value at grant date, consistent with the method prescribed by FAS 123, net income and earnings per share would have been reduced to the pro forma amounts as follows:

|  | <u>Three Months Ended</u> |                          | <u>Six Months Ended</u>  |                          |
|--|---------------------------|--------------------------|--------------------------|--------------------------|
|  | <b>July 29,<br/>2005</b>  | <b>July 30,<br/>2004</b> | <b>July 29,<br/>2005</b> | <b>July 30,<br/>2004</b> |
| Net income, as reported  |                           | \$                       | \$                       | \$                       |
|  | \$ 482,000                | 903,000                  | 931,000                  | 1,112,000                |
| Deduct:  |                           |                          |                          |                          |
| Total stock-based employee compensation determined under fair value based method |                           |                          |                          |                          |
| for all awards, net of reflected tax effects                                     | (4,000)                   | -                        | (4,000)                  | -                        |
| Pro forma net income   |                           | \$                       | \$                       | \$                       |
|  | \$ 478,000                | 903,000                  | 927,000                  | 1,112,000                |
| Earnings per share:  |                           |                          |                          |                          |
| Basic as reported  |                           |                          |                          |                          |
|  | \$ 0.12                   | \$ 0.23                  | \$ 0.24                  | \$ 0.28                  |
| Basic pro forma  |                           |                          |                          |                          |
|  | \$ 0.12                   | \$ 0.23                  | \$ 0.24                  | \$ 0.28                  |
| Diluted as reported  |                           |                          |                          |                          |
|  | \$ 0.12                   | \$ 0.23                  | \$ 0.24                  | \$ 0.28                  |

Diluted pro forma

\$ 0.12

\$ 0.23

\$ 0.24

\$ 0.28

**Note 8 Earnings per Share**

For the three months and six months ended July 29, 2005, 32,500 stock options were excluded from the calculation of shares applicable to diluted net income per share because their inclusion would have been anti-dilutive. No stock options were outstanding for the corresponding periods of the prior year.

**Note 9 Commitments, Contingencies and Subsequent Events**

In accordance with a consent agreement with the Department of Environmental Protection signed by the Company in 1993, the Company's environmental consultant has developed an interim remedial action plan to contain and remediate certain contamination on and underlying the Company's property in Clearwater, Florida. During 1997, the Company recorded a provision of approximately \$175,000 related to the estimated costs to be incurred under this plan. As of January 31, 2000, the Company had utilized all amounts originally recorded in other accrued expenses, and Phase I remediation had been completed.



During the third quarter of 2001, management determined the post-remediation monitoring expense related to the environmental cleanup of 1993 would cost approximately \$125,000. This amount was accrued and expensed during the third quarter of 2001. As of January 31, 2004, all existing reserve balances had been utilized. Based upon information provided by the Company's environmental consultants, management estimates that the Company will incur post-remediation monitoring expenses of approximately \$38,000, for which a reserve has been established as of January 31, 2004. An assessment of this reserve was made as of January 31, 2005, and based upon the estimated cost of the remaining remediation, the reserve was increased to approximately \$98,000. A subsequent assessment of activities completed and estimated remaining remediation was made as of July 29, 2005, and the reserve was reduced to approximately \$93,000 as of that date.

The Company's contractual obligations for future minimum payments under our purchase commitments, long-term debt and operating leases as of July 29, 2005 are as follows:

| <b>Contractual Obligations</b> | <b>Total</b>        | <b><u>Payments Due by Period</u></b> |                    |                    |                     |
|--------------------------------|---------------------|--------------------------------------|--------------------|--------------------|---------------------|
|                                |                     | <b>Less than One Year</b>            | <b>1 - 3 years</b> | <b>4 - 5 years</b> | <b>&gt; 5 years</b> |
| Purchase commitments           | \$ 4,741,000        | \$ 4,579,000                         | \$ 145,000         | \$ 17,000          | \$ -                |
| Long-term debt                 | 2,909,000           | 230,000                              | 460,000            | 460,000            | 1,759,000           |
| Operating leases               | 618,000             | 393,000                              | 225,000            | -                  | -                   |
| <b>Total</b>                   | <b>\$ 8,268,000</b> | <b>\$ 5,202,000</b>                  | <b>\$ 830,000</b>  | <b>\$ 477,000</b>  | <b>\$ 1,759,000</b> |

A securities class action lawsuit in the Federal District Court of the Middle District of Florida remains pending against the Company, PricewaterhouseCoopers LLP, the Company's former auditor, and four former employees of the Company, two of whom were directors (the **Federal Class Action**). On April 1, 2005, the Company and the other named defendants in the Federal Class Action filed a Notice of Settlement with the court. On July 13, 2005, all parties filed a Stipulation of Settlement (the **Stipulation**) to settle the Federal Class Action. The Stipulation provides for a payment by or on behalf of the defendants to the plaintiffs of approximately \$5.35 million. Of this amount, the Company is obligated to pay \$800,000, which has been accrued in the accompanying consolidated financial statements as of July 29, 2005 and January 31, 2005. The balance of the settlement is expected to be paid by Zurich American Insurance Company on behalf of the Company and the individual defendants under the Company's directors and officers' insurance policy, and by PricewaterhouseCoopers LLP. On August 9, 2005, the court preliminarily approved the settlement and set a fairness hearing on November 18, 2005 to consider final approval of the settlement. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

On April 6, 2005, Aerosonic became aware of the Franzitta Suit filed on March 21, 2005 in the Circuit Court of Hillsborough County, Florida. The Franzitta Suit alleges (a) breaches of fiduciary duties and aiding and abetting such breaches by the present and former directors, officers, and employees named as defendants, for an asserted "Relevant Period" which appears to begin sometime in 1999 and continues to the present time; and (b) breaches of contract, professional negligence, and aiding and abetting breaches of fiduciary duties, by the Company's former registered independent certified public accounting firm during the asserted Relevant Period, and that firm's partner in charge of

the Company's audits during most of that time.

On July 11, 2005, the plaintiffs voluntarily dismissed their claims against William Parker, a former director of the Company. On July 25, 2005, all parties filed a Stipulation of Settlement to settle the Franzitta Suit (the "Franzitta Stipulation"). The settlement provides the Company appoint a new independent director to its board and grant standing authority to the Company's Audit Committee to investigate any matters it deems appropriate. The settlement also provides for a payment of up to \$75,000 in attorney's fees and costs to plaintiff's counsel, none of which is required to be paid by the Company. On August 16, 2005, the court preliminarily approved the settlement and set a final fairness hearing on November 21, 2005. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

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**Item 2**

**Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A )**

**Results of Operations**

Revenues for the second quarter increased approximately \$1,040,000 when compared to the second quarter of fiscal year 2005. Increases in core instrument revenues of approximately \$1,853,000 were offset by decreases in revenues from repairs and spare parts of approximately \$298,000, and continuing slower progress on the Joint Strike Fighter ( JSF ) development program of approximately \$515,000.

Revenues for the six months ended July 29, 2005 increased approximately \$3,019,000 when compared to the six months ended July 30, 2004. Increases in core instrument revenues of approximately \$4,071,000 were offset by decreases in revenues from repairs and spare parts of approximately \$224,000, and continuing slower progress on the JSF development program of approximately \$828,000.

Gross profit for the three months ended July 29, 2005 increased by approximately 11%, or approximately \$294,000, when compared to the second quarter of fiscal year 2005. Approximately \$356,000 of this change is due to an increase in volume, with an offset of approximately \$62,000 due to changes in the revenue mix due to revenue increases in core instruments and revenue reductions in repairs and spare parts that yield higher margins.

Gross profit for the six months ended July 29, 2005 increased by approximately 17%, or approximately \$811,000, when compared to the six months ended July 30, 2004. A volume-related increase in gross profit margin of approximately \$949,000 was partially offset by a decrease in gross profit margin of approximately \$138,000 due to changes in the revenue mix.

Selling, general and administrative expenses for the second quarter decreased approximately \$98,000 when compared to the three months ended July 30, 2004. This decrease is primarily attributable to the reductions in outside engineering costs of approximately \$126,000 and reductions in compensation expense of approximately \$32,000. These decreases were partially offset by an increase in insurance costs of approximately \$26,000, an increase in advisory fees of approximately \$22,000 and loan amortization costs of approximately \$12,000.

Selling, general and administrative expenses for the six months ended July 29, 2005 decreased approximately \$64,000 when compared to the six months ended July 30, 2004. This decrease is primarily attributable to the reductions in outside engineering costs of approximately \$106,000 and reductions in corporate governance expenses of approximately \$55,000. These decreases were partially offset by an increase in insurance costs of approximately \$52,000 as well as an increase in advisory fees of approximately \$45,000.

Interest expense decreased approximately \$16,000 for the three months ended July 29, 2005 when compared to the three months ended July 30, 2004. This decrease is due to lower average debt balances.

Interest expense increased approximately \$21,000 for the six months ended July 29, 2005 when compared to the six months ended July 30, 2004. This increase is partially due to higher interest rates and is partially offset by lower average debt balances.

Miscellaneous income decreased approximately \$1,073,000 for the three months ended July 29, 2005 when compared to the three months ended July 30, 2004. The Company received a non-recurring insurance settlement in the second quarter of fiscal year 2005 of approximately \$997,000. The remainder of the difference results from the strengthening of the U.S. Dollar against the British Pound versus a weakening of the dollar against the pound during the three months ended July 29, 2005.

Miscellaneous income decreased approximately \$1,139,000 for the six months ended July 29, 2005 when compared to the six months ended July 30, 2004. This decrease is primarily due to the insurance recovery described in the preceding paragraph as well as the Company's sale of its Engine Vibration Monitoring System ( **EVMS** ) product line inventory in February 2004 that resulted in miscellaneous income of approximately \$170,000.

Income tax expense decreased approximately \$244,000 for the three months ended July 29, 2005 when compared to the three months ended July 30, 2004. The decrease was due to lower taxable income for the current period.

Income tax expense decreased approximately \$104,000 for the six months ended July 29, 2005 when compared to the six months ended July 30, 2004. The decrease was due to lower taxable income for the current period.

## Liquidity and Capital Resources

Cash provided by operating activities was approximately \$2,246,000 for the six months ended July 29, 2005 an increase of approximately \$3,093,000 when compared to cash provided during the six months ended July 30, 2004. This increase in cash provided is primarily attributable to:

An increase due to accounts payable of approximately \$2,233,000 as the Company withheld a payment to a vendor of approximately \$685,000 pending the settlement of a dispute. In addition, significant one-time payments of professional fees in fiscal year 2005 did not recur.

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An increase due to the reduction of costs less estimated losses in excess of billings of approximately \$1,751,000 resulting from the achievement of milestones for the JSF program as well as a reduced rate of revenue recognition for the program.

.

An increase due to accrued expenses and other liabilities of approximately \$749,000 primarily due to the Company's recording of its anticipated settlement of its class action litigation of approximately \$800,000.

.

An increase due to allowances for doubtful accounts of approximately \$140,000 as the charge that was incurred during fiscal year 2005 did not recur.

These increases in cash provided were partially offset by:

.

A decrease in net income of approximately \$181,000.

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A decrease due to accrued compensation and benefits of approximately \$237,000.

A decrease of approximately \$986,000 due to a comparative period-over-period increase in accounts receivable that resulted from higher revenue.

A decrease of approximately \$348,000 due to a comparative period-over-period increase in inventory accumulation, as a result of higher volume.

Cash used in investing activities increased approximately \$51,000 due to higher investment in Machinery and Equipment.

Cash used by financing activities increased approximately \$279,000 as the Company reduced its outstanding debt.

Future capital requirements depend on numerous factors, including research and development, expansion of product lines, the resolution of the recently filed class action suits and potential related litigation, and other factors. Management believes that cash and cash equivalents, together with the Company's current borrowing arrangements will provide for these necessary expenditures. Furthermore, the Company may develop and introduce new or enhanced products, respond to competitive pressures, invest or acquire businesses or technologies or respond to unanticipated requirements or developments, which would require additional resources.

The Company's ability to maintain sufficient liquidity in fiscal year 2006 and beyond is highly dependent upon achieving expected operating results. Failure to successfully achieve these results could have a material adverse effect on the Company's liquidity and operations in fiscal year 2006, and could require implementation of further measures, including deferring planned capital expenditures, reducing discretionary spending, and/or, if necessary, selling assets.

### ***Critical Accounting Policies***

The discussion and analysis of our financial condition and results of operations are based upon the accompanying unaudited condensed consolidated financial statements, which have been prepared in accordance with accounting principals generally accepted in the United States. The preparation of those financial statements and this Quarterly Report on Form 10-Q requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure items, including disclosure of contingent assets and liabilities, at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions, and as a result of trends and uncertainties identified above under **RESULTS OF OPERATIONS** and **LIQUIDITY AND CAPITAL RESOURCES** . Further, such differences could be material.



Set forth below is a discussion of the Company's critical accounting policies. The Company considers critical accounting policies to be those (i) that require the Company to make estimates that are highly uncertain at the time the estimate is made, (ii) for which a different estimate which could have been made would have a material impact on the Company's financial statements, (iii) that are the most important and pervasive policies utilized, and (iv) that are the most sensitive to material change from external factors. Additionally, the policies discussed below are critical to an understanding of the financial statements because their application places the most significant demands on management's judgment, with financial reporting results relying on estimates about the effect of matters that are highly uncertain. Specific risks for these critical accounting policies are described in the following paragraphs. The impact and any associated risks related to these policies on business operations is discussed throughout this MD&A where such policies affect reported and expected financial results.

Senior management has discussed the development and selection of the critical accounting estimates and the related disclosure included herein with the Audit Committee of the Board of Directors.

### ***Revenue Recognition***

The Company manufactures most of its products on a build-to-order basis and ships products upon completion. The Company has a policy of strict adherence to the provisions of SEC Staff Accounting Bulletin 104 ( **SAB 104** ) in order to accurately state its revenues in each accounting period. For certain situations, some judgment is required, but most sales have clear revenue recognition criteria.

Revenue sources for product sales are largely from sales to commercial and government customers. The majority of customer sales terms are F.O.B. origin, although some customer terms are F.O.B. destination. For those customers where terms are origin, revenue is generally recognized upon shipment, unless additional prevailing factors would not be in accordance with the revenue recognition requirements of SAB 104. For those customers whose terms are destination, revenue is generally not recognized until goods arrive at the customers' premises and all other revenue recognition criteria are met.

The Company experiences a certain degree of sales returns that varies over time. Generally such returns occur within no more than 90 days after shipment by the Company to its customers. In accordance with Statement of Financial Accounting Standards No. 48 ( **SFAS 48** ) Revenue Recognition When Right of Return Exists, the Company is able to make a reasonable estimation of expected sales returns based upon history and as contemplated by the requirements of SFAS 48. For example, sales returns may occur if delivery schedules are changed by customers after products have shipped or if products are received by customers but do not meet specifications. In such cases, customers may choose to return products to the Company. Absent such circumstances, customers do not have a right to return products if the Company has met all contractual obligations. The Company has established a sales return reserve that approximates an expected level of sales returns over a 90-day period.



From time to time, the Company will jointly develop products with its customers for future applications. In such circumstances, the Company recognizes revenue on a percentage of completion basis, measured by the percentage of costs incurred to date to estimated total costs for the contract. This method is used because management considers expended costs to be the best available measure of progress on the contracts. The percentage of completion contract costs include direct labor, material, subcontracting costs, test facilities, and other indirect costs as allocated. Other operating costs are charged to expense as incurred. During fiscal 2003, the Company secured one long-term fixed-price contract for the development of instrumentation for the JSF program.

Occasionally the Company enters into research and development contracts with customers. The Company accounts for such contracts on the basis of the lesser of non-refundable cash versus percentage of completion.

***Accounts Receivable Allowance for Doubtful Accounts and Credit Losses***

The Company continuously evaluates its customers and provides reserves for anticipated credit losses as soon as collection becomes compromised. The Company does maintain a limited reserve in anticipation that smaller accounts may become a collection issue, which occurs from time to time based on historical experience. However, most of the Company's customers are financially sound and the Company's history of bad debts is relatively low. While credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same credit loss rates that have been experienced in the past. Measurement of such losses requires consideration of historical loss experience, including the need to adjust for current conditions, and judgments about the probable effects of relevant observable data, including present economic conditions such as delinquency rates and financial health of specific customers.

***Provisions for Excess and Obsolete Inventory Losses and Residual Value Losses***

The Company values inventory at the lower of cost (using a method that approximates the first-in, first-out method) or net realizable value. Reviews of inventory quantities on hand have been conducted to determine if usage or sales history supports maintaining inventory values at full cost or if it has instead become necessary to record a provision for slow moving, excess and obsolete inventory based primarily on estimated forecasts of product demand and production requirements for the subsequent twelve months. Estimates of future product demand may prove to be inaccurate, in which case the Company may understate or overstate the provision required for excess and obsolete inventory. Although the Company endeavors to ensure the accuracy of forecasts of future product demand, any significant unanticipated changes in demand or technological developments could have a significant impact on the value of inventory and consequently reported operating results.

***Work In Process Inventories***

Management employs certain methods to estimate the value of work in process inventories for financial reporting purposes. Company practice has been to conduct cycle counts of inventory at its Clearwater, Florida, Earlysville, Virginia and Wichita, Kansas operations throughout the year. Generally, for items that are in process at the end of a fiscal year, management will make an estimate during the cycle counting process regarding the percentage of completion of such items in order to accurately reflect costs incurred to date on the production of the items that are still in process. These estimates are affected by the nature of the operation at which the items are located at the time a physical inventory is conducted, and are subject to judgment.

***Manufacturing Overhead Cost Application***

The Company establishes its inventoriable cost of manufacturing overhead by calculating its overhead costs as a percentage of direct labor and applying that percentage to direct labor that has been charged to inventory on a twelve month rolling average basis. This application percentage is reviewed at least quarterly and is adjusted at least annually.

#### *Deferred Tax Asset Valuation Allowance*

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards ( **SFAS** ) No. 109, Accounting for Income Taxes. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. A valuation allowance is provided against the future benefit of deferred tax assets if it is determined that it is more likely than not that the future tax benefits associated with the deferred tax asset will not be realized.

#### *Long-Lived Assets*

Management periodically evaluates long-lived assets for potential impairment and will record an impairment charge whenever events or changes in circumstances indicate the carrying amount of the assets may not be fully recoverable. As of July 29, 2005 and January 31, 2005, management does not believe that any assets are impaired.

The Company will capitalize production costs for computer software that is to be utilized as an integral part of a product when both (a) technological feasibility is established for the software and (b) all research and development activities for the other components of the product have been completed. Amortization is charged to expense at the greater of the expected unit sales versus units sold or the straight line method for a period of three years from the date the product becomes available for general release to customers.

***Other Accounts Affected by Management Estimates***

From time to time, management will utilize estimates when preparing the financial statements of the Company. Such areas include allowances for doubtful accounts, reserves for warranty and sales returns, depreciation, amortization and other accruals.

The Company has established a provision for warranty claims in anticipation of a certain degree of warranty activity, which generally is a minimal expense. This provision is based upon recent warranty experience.

Management also uses estimates in calculating the percentage of completion of the JSF program. These estimates have a significant impact on Costs less estimated losses in excess of billings included in the Company's consolidated balance sheets.

***Off-Balance Sheet Arrangements***

The Company does not maintain off-balance sheet arrangements nor does it participate in non-exchange traded contracts requiring fair value accounting treatment.

***Contractual Obligations***

The Company's contractual obligations for future minimum payments under our purchase commitments, long-term debt and operating leases as of July 29, 2005 are as follows:

| <b>C o n t r a c t u a l<br/>Obligations</b> | <b>Total</b> | <b><u>Payments Due by Period</u></b> |                    |                    |                     |
|--|--------------|--------------------------------------|--------------------|--------------------|---------------------|
|  |              | <b>Less than<br/>One Year</b>        | <b>1 - 3 years</b> | <b>4 - 5 years</b> | <b>&gt; 5 years</b> |
| Purchase commitments                         | \$ 4,741,000 | \$ 4,579,000                         | \$ 145,000         | \$ 17,000          | -                   |
| Long-term debt                               | 2,909,000    | 230,000                              | 460,000            | 460,000            | 1,759,000           |
| Operating leases                             | 618,000      | 393,000                              | 225,000            | -                  | -                   |
| <b>Total</b>                                 | \$ 8,268,000 | \$ 5,202,000                         | \$ 830,000         | \$ 477,000         | \$ 1,759,000        |

**Item 3**

**Quantitative and Qualitative Disclosures about Market Risk.**

The primary market risk exposure for the Company is interest rate risk under the Company's variable rates in its loans from Wachovia discussed in Note 6 to its Financial Statements in Part I above. The Company does not currently utilize any financial instruments to manage interest rate risk.

**Item 4**

**Controls and Procedures.**

As of July 29, 2005, Aerosonic's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of Aerosonic's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) and concluded that such disclosure controls and procedures were effective as of such date.

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### **PART II OTHER INFORMATION**

#### **ITEM 1. LEGAL PROCEEDINGS**

##### **Class Action Litigation**

On November 12, 2003, a class action lawsuit was filed in the United States District Court for the Middle District of Florida by Sebastian P. Gaeta, individually and on behalf of all other similarly situated (the **Gaeta Suit**), against the Company, PricewaterhouseCoopers LLP, the Company's former independent registered certified public accounting firm, J. Mervyn Nabors, a former director and former President and CEO of the Company, Eric J. McCracken, a former Chief Financial Officer of the Company, and Michael T. Reed, a former Controller of the Company. The action alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the **Exchange Act**) and Rule 10b-5 promulgated under that act, including, among other things, that the Company made materially false statements concerning the Company's financial condition and its future prospects. The plaintiff alleges that he suffered damages as the result of his purchase and sale of the Company's Common Stock during the asserted Class Period from November 13, 1998 through March 17, 2003. The action seeks compensatory and other damages, and costs and expenses associated with the litigation.

Shortly after the Gaeta Suit was filed, two other putative class actions (the "**Pratsch Suit**" and "**Suarez Suit**") were filed against the same defendants as in the Gaeta Suit and predicated upon alleged violations of the same securities laws, asserting that plaintiffs purchased the Company's stock at artificially inflated prices during the Class Period and have been damaged thereby. The Pratsch Suit and Suarez Suit assert a Class Period from May 3, 1999 through March 17, 2003. At a February 27, 2004 hearing, plaintiffs in the Suarez Suit voluntarily withdrew their complaint. On February 27, 2004, the Court entered an order consolidating the Gaeta Suit and Pratsch Suit into one case entitled "In re Aerosonic Corporation Securities Litigation" (the **Federal Class Action**), appointing Lead Plaintiffs (the "Miville Group") and approving the selection of Lead Plaintiffs' Counsel (Berger & Montague P.C.).

On April 27, 2004, Lead Plaintiffs filed an amended and consolidated class action complaint that alleges violation of Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 including, among other things, that the Company made materially false statements concerning the Company's financial condition and its future prospects. The amended complaint also added as a defendant, Andrew Norstrud, a former employee of the Company. On June 28, 2004, the Company responded to the amended complaint by filing a motion to dismiss, and each of the other defendants also moved to dismiss the amended complaint. On August 27, 2004 Lead Plaintiffs filed a memorandum of law as a comprehensive opposition to the motion to dismiss.

On April 1, 2005, the Company and the other named defendants in the Federal Class Action filed a Notice of Settlement with the court. On July 13, 2005, all parties filed a Stipulation of Settlement (the **Stipulation**) to settle the Federal Class Action. The Stipulation provides for a payment by or on behalf of the defendants to the plaintiffs of

approximately \$5.35 million. Of this amount, the Company is obligated to pay \$800,000, which has been accrued in the accompanying consolidated financial statements as of July 29, 2005 and January 31, 2005. The balance of the settlement is expected to be paid by Zurich American Insurance Company on behalf of the Company and the individual defendants under the Company's directors' and officers' insurance policy, and by PricewaterhouseCoopers LLP. On August 9, 2005, the court preliminarily approved the settlement and set a fairness hearing on November 18, 2005 to consider final approval of the settlement. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

### **Derivative Suit**

On April 6, 2005, Aerosonic became aware of a Derivative Complaint (the **Franzitta Suit**) filed on March 21, 2005 in the Circuit Court of Hillsborough County, Florida, by Matilda Franzitta, asserting that she is a shareholder acting on behalf of the Company, which is a nominal defendant, and naming as defendants certain present and past officers, directors and employees, some of whom also were named as defendants in the Federal Class Action, and the Company's former auditor and that firm's partner in charge of certain of the Company's audits.

The Franzitta Suit alleges (a) breaches of fiduciary duties and aiding and abetting such breaches by the present and former directors, officers, and employees named as defendants, for an asserted "Relevant Period" which appears to begin sometime in 1999 and continues to the present time; and (b) breaches of contract, professional negligence, and aiding and abetting breaches of fiduciary duties, by the Company's former registered independent certified public accounting firm during the asserted Relevant Period, and that firm's partner in charge of the Company's audits during most of that time.

On July 11, 2005, the plaintiffs voluntarily dismissed their claims against William Parker, a former director of the Company. On July 25, 2005, all parties filed a Stipulation of Settlement to settle the Franzitta Suit (the Franzitta Stipulation). The settlement provides the Company appoint a new independent director to its board and grant standing authority to the Company's Audit Committee to investigate any matters it deems appropriate. The settlement also provides for a payment of up to \$75,000 in attorney's fees and costs to plaintiff's counsel, none of which is required to be paid by the Company. On August 16, 2005, the court preliminarily approved the settlement and set a final fairness hearing on November 21, 2005. The settlement is subject to final court approval, as well as certain other conditions that may cause the settlement not to be consummated.

#### **Additional Proceedings and Matters**

In addition to the foregoing, from time to time, the Company is involved in certain claims and legal actions arising in the ordinary course of business. In the opinion of management, at this time, there are no claims or legal actions that will have a material adverse effect on the Company's financial position, results of operations, or liquidity.

#### **ITEM 2. UNREGISTERED SALE OF SECURITIES AND USE OF PROCEEDS**

None

#### **ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None

#### **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None

#### **ITEM 5. OTHER INFORMATION**

None

#### **ITEM 6. EXHIBITS**



**Exhibit No.**

**Description of Exhibit**

31.1

Section 302 Certifications

31.2

Section 302 Certifications

32.1

Section 906 Certifications

32.2

Section 906 Certifications

**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.

Date:

August 26, 2005

**AEROSONIC CORPORATION**

/s/ David A. Baldini

David A. Baldini, President and Chief Executive Officer

Date:

August 26, 2005

**AEROSONIC CORPORATION**

/s/ Gary E. Colbert

Gary E. Colbert, Chief Financial Officer

**CERTIFICATIONS**

I, David A. Baldini, certify that:

1.

I have reviewed this Quarterly report on Form 10-Q of Aerosonic Corporation;

2.

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

3.

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

4.

The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

(a)

Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b)

Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c)

Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5.

The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a)

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

(b)

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

Date:

August 26, 2005

/s/ David A. Baldini

David A. Baldini

President and Chief Executive Officer

**CERTIFICATIONS**

I, Gary E. Colbert, certify that:

1.

I have reviewed this Quarterly report on Form 10-Q of Aerosonic Corporation;

2.

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

3.

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

4.

The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

(a)

Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b)

Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c)

Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5.

The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a)

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

(b)

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

Date:

August 26, 2005

/s/ Gary E. Colbert

Gary E. Colbert

Chief Financial Officer

**AEROSONIC CORPORATION**

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Aerosonic Corporation (the **registrant** ) on Form 10-Q for the period ending July 29, 2005 as filed with the Securities and Exchange Commission on the date hereof (the **report** ), I, David A. Baldini, Chief Executive Officer of the registrant, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1)

The report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934: and

(2)

The information contained in the report fairly presents, in all material respects, the financial condition and result of operations of the registrant.

Date:

August 26, 2005

/s/ David A. Baldini

David A. Baldini

President and Chief Executive Officer

**AEROSONIC CORPORATION**

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Aerosonic Corporation (the **registrant** ) on Form 10-Q for the period ending July 29, 2005 as filed with the Securities and Exchange Commission on the date hereof (the **report** ), I, Gary E. Colbert, Chief Financial Officer of the registrant, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1)

The report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934: and

(2)

The information contained in the report fairly presents, in all material respects, the financial condition and result of operations of the registrant.

Date:

August 26, 2005

/s/ Gary E. Colbert

Gary E. Colbert

Chief Financial Officer