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

FORM 10-Q

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

For the quarterly period ended March 31, 2022

OR

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

Commission File Number 1-4383



ESPEY MFG. & ELECTRONICS CORP.

(Exact name of registrant as specified in its charter)

NEW YORK
(State of incorporation)

Trading Symbol
ESP

14-1387171
(I.R.S. Employer's Identification No.)

233 Ballston Avenue, Saratoga Springs, New York 12866

(Address of principal executive offices)

518-245-4400

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically 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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company:

Large accelerated filer
 Accelerated filer

Non-accelerated filer
 Smaller reporting company
 Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Securities Exchange Act.

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

Yes No

At May 12, 2022, there were 2,702,633 shares outstanding of the registrant's Common stock, \$.33-1/3 par value.

ESPEY MFG. & ELECTRONICS CORP.
Quarterly Report on Form 10-Q
I N D E X

<u>PART I</u>	<u>FINANCIAL INFORMATION</u>	<u>PAGE</u>
<u>Item 1</u>	<u>Financial Statements:</u>	
	<u>Balance Sheets - March 31, 2022 (Unaudited) and June 30, 2021</u>	1
	<u>Statements of Comprehensive Income (Loss) (Unaudited) - Three and Nine Months Ended March 31, 2022 and 2021</u>	2
	<u>Statements of Changes in Stockholders' Equity (Unaudited) - Three and Nine Months Ended March 31, 2022 and 2021</u>	3
	<u>Statements of Cash Flows (Unaudited) - Nine Months Ended March 31, 2022 and 2021</u>	7
	<u>Notes to Financial Statements (Unaudited)</u>	8
<u>Item 2</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	14
<u>Item 3</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	20
<u>Item 4</u>	<u>Controls and Procedures</u>	20
<u>PART II</u>	<u>OTHER INFORMATION</u>	21
<u>Item 1</u>	<u>Legal Proceedings</u>	21
<u>Item 2</u>	<u>Unregistered Sales of Equity Securities</u>	21
<u>Item 3</u>	<u>Defaults Upon Senior Securities</u>	21
<u>Item 4</u>	<u>Mine Safety Disclosures</u>	21
<u>Item 5</u>	<u>Other Information</u>	21
<u>Item 6</u>	<u>Exhibits</u>	21
	<u>SIGNATURES</u>	22

PART I: FINANCIAL INFORMATION
ESPEY MFG. & ELECTRONICS CORP.
Balance Sheets

March 31, 2022 (Unaudited) and June 30, 2021

	March 31, 2022	June 30, 2021
ASSETS		
Cash and cash equivalents	\$ 7,282,832	\$ 6,802,712
Investment securities	3,209,297	3,092,000
Trade accounts receivable, net of allowance of \$3,000	5,642,869	5,353,781
Income tax receivable	91,163	249,602
Inventories:		
Raw materials	2,142,025	2,111,058
Work-in-process	259,932	326,198
Costs related to contracts in process	16,542,146	16,354,636
Total inventories	18,944,103	18,791,892
Prepaid expenses and other current assets	928,836	700,297
Total current assets	36,099,100	34,990,284
Property, plant and equipment, net	2,833,188	2,990,519
Total assets	\$ 38,932,288	\$ 37,980,803
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable	\$ 2,098,248	\$ 2,718,173
Accrued expenses:		
Salaries and wages	577,154	475,667
Vacation	752,457	672,611
ESOP payable	245,362	—
Other	271,803	126,014
Payroll and other taxes withheld	58,957	409,881
Contract liabilities	3,354,066	3,077,605
Total current liabilities	7,358,047	7,479,951
Deferred tax liabilities	118,221	168,557
Total liabilities	7,476,268	7,648,508
Commitments and contingencies (See Note 5)		
Common stock, par value \$.33-1/3 per share		
Authorized 10,000,000 shares; Issued 3,129,874 shares as of March 31, 2022 and June 30, 2021. Outstanding 2,702,633 shares as of March 31, 2022 and June 30, 2021 (includes 262,077 and 279,429 Unearned ESOP shares, respectively)	1,043,291	1,043,291
Capital in excess of par value	23,160,362	23,026,096
Accumulated other comprehensive loss	(1,523)	(2,361)
Retained earnings	18,403,351	17,414,730
	42,605,481	41,481,756
Less: Unearned ESOP shares	(5,110,770)	(5,110,770)
Cost of 427,241 shares of common stock in treasury as of March 31, 2022 and June 30, 2021	(6,038,691)	(6,038,691)
Total stockholders' equity	31,456,020	30,332,295
Total liabilities and stockholders' equity	\$ 38,932,288	\$ 37,980,803

The accompanying notes are an integral part of the financial statements.

ESPEY MFG. & ELECTRONICS CORP.
 Statements of Comprehensive Income (Loss) (Unaudited)
 Three and Nine Months Ended March 31, 2022 and 2021

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
Net sales	\$ 8,620,049	\$ 4,205,068	\$ 23,623,531	\$ 18,432,648
Cost of sales	6,885,169	4,392,222	19,328,736	16,778,967
Gross profit (loss)	1,734,880	(187,154)	4,294,795	1,653,681
Selling, general and administrative expenses	933,725	990,311	3,114,715	2,850,415
Operating income (loss)	801,155	(1,177,465)	1,180,080	(1,196,734)
Other income				
Interest income	2,987	2,486	6,299	19,456
Other	2,674	4,589	30,750	21,450
Total other income	5,661	7,075	37,049	40,906
Income (loss) before provision (benefit) for income taxes	806,816	(1,170,390)	1,217,129	(1,155,828)
Provision (benefit) for income taxes	145,457	(100,276)	228,508	(94,531)
Net income (loss)	\$ 661,359	\$ (1,070,114)	\$ 988,621	\$ (1,061,297)
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on investment securities	838	(167)	838	871
Total comprehensive income (loss)	\$ 662,197	\$ (1,070,281)	\$ 989,459	\$ (1,060,426)
Net income (loss) per share:				
Basic	\$ 0.27	\$ (0.44)	\$ 0.41	\$ (0.44)
Diluted	\$ 0.27	\$ (0.44)	\$ 0.41	\$ (0.44)
Weighted average number of shares outstanding:				
Basic	2,434,836	2,405,670	2,429,009	2,403,641
Diluted	2,434,836	2,405,670	2,429,059	2,403,641
Dividends per share:	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.50

The accompanying notes are an integral part of the financial statements.

Espey Mfg. & Electronics Corp.
 Statements of Changes in Stockholders' Equity (Unaudited)
 Three Months Ended March 31, 2022

	Outstanding Shares	Common Amount	Capital in Excess of Par Value	Accumulated Other Comprehensive (Loss) Income	Retained Earnings	Treasury Shares	Treasury Amount	Unearned ESOP Shares	Total Stockholders' Equity
Balance as of December 31, 2021	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,120,663</u>	<u>\$ (2,361)</u>	<u>\$ 17,741,992</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,110,770)</u>	<u>\$ 30,754,124</u>
Comprehensive income:									
Net income					<u>661,359</u>				<u>661,359</u>
Other comprehensive income, net of tax of \$176				<u>838</u>					<u>838</u>
Total comprehensive income									<u>662,197</u>
Stock-based compensation			<u>39,699</u>						<u>39,699</u>
Balance as of March 31, 2022	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,160,362</u>	<u>\$ (1,523)</u>	<u>\$ 18,403,351</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,110,770)</u>	<u>\$ 31,456,020</u>

The accompanying notes are an integral part of the financial statements.

Espey Mfg. & Electronics Corp.
 Statements of Changes in Stockholders' Equity (Unaudited)
 Nine Months Ended March 31, 2022

	Outstanding Shares	Common Amount	Capital in Excess of Par Value	Accumulated Other Comprehensive (Loss) Income	Retained Earnings	Treasury Shares	Treasury Amount	Unearned ESOP Shares	Total Stockholders' Equity
Balance as of June 30, 2021	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,026,096</u>	<u>\$ (2,361)</u>	<u>\$ 17,414,730</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,110,770)</u>	<u>\$ 30,332,295</u>
Comprehensive income:									
Net income					<u>988,621</u>				<u>988,621</u>
Other comprehensive income, net of tax of \$176				<u>838</u>					<u>838</u>
Total comprehensive income									<u>989,459</u>
Stock-based compensation			<u>134,266</u>						<u>134,266</u>
Balance as of March 31, 2022	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,160,362</u>	<u>\$ (1,523)</u>	<u>\$ 18,403,351</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,110,770)</u>	<u>\$ 31,456,020</u>

The accompanying notes are an integral part of the financial statements.

Espey Mfg. & Electronics Corp.
 Statements of Changes in Stockholders' Equity (Unaudited)
 Three Months Ended March 31, 2021

	Outstanding Shares	Common Amount	Capital in Excess of Par Value	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Shares	Treasury Amount	Unearned ESOP Shares	Total Stockholders' Equity
Balance as of December 31, 2020	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 22,995,640</u>	<u>\$ (2,069)</u>	<u>\$ 17,605,090</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,487,000)</u>	<u>\$ 30,116,261</u>
Comprehensive loss:									
Net loss					<u>(1,070,114)</u>				<u>(1,070,114)</u>
Other comprehensive loss, net of tax of \$ (44)				<u>(167)</u>					<u>(167)</u>
Total comprehensive loss									<u>(1,070,281)</u>
Stock-based compensation			<u>25,412</u>						<u>25,412</u>
Balance as of March 31, 2021	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,021,052</u>	<u>\$ (2,236)</u>	<u>\$ 16,534,976</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,487,000)</u>	<u>\$ 29,071,392</u>

The accompanying notes are an integral part of the financial statements.

Espey Mfg. & Electronics Corp.
 Statements of Changes in Stockholders' Equity (Unaudited)
 Nine Months Ended March 31, 2021

	Outstanding Shares	Common Amount	Capital in Excess of Par Value	Accumulated Other Comprehensive (Loss) Income	Retained Earnings	Treasury Shares	Treasury Amount	Unearned ESOP Shares	Total Stockholders' Equity
Balance as of June 30, 2020	<u>2,402,633</u>	<u>\$ 1,009,958</u>	<u>\$ 19,073,213</u>	<u>\$ (3,107)</u>	<u>\$ 18,797,589</u>	<u>627,241</u>	<u>\$ (7,650,805)</u>	<u>\$ —</u>	<u>\$ 31,226,848</u>
Comprehensive loss:									
Net loss					<u>(1,061,297)</u>				<u>(1,061,297)</u>
Other comprehensive income, net of tax of \$ 232				<u>871</u>					<u>871</u>
Total comprehensive loss									<u>(1,060,426)</u>
Stock-based compensation			<u>106,286</u>						<u>106,286</u>
Dividends paid on common stock \$0.50 per share					<u>(1,201,316)</u>				<u>(1,201,316)</u>
Sales of stock to ESOP	<u>300,000</u>	<u>33,333</u>	<u>3,841,553</u>			<u>(200,000)</u>	<u>1,612,114</u>	<u>(5,487,000)</u>	<u>—</u>
Balance as of March 31, 2021	<u>2,702,633</u>	<u>\$ 1,043,291</u>	<u>\$ 23,021,052</u>	<u>\$ (2,236)</u>	<u>\$ 16,534,976</u>	<u>427,241</u>	<u>\$ (6,038,691)</u>	<u>\$ (5,487,000)</u>	<u>\$ 29,071,392</u>

The accompanying notes are an integral part of the financial statements.

ESPEY MFG. & ELECTRONICS CORP.
Statements of Cash Flows (Unaudited)
Nine Months Ended March 31, 2022 and 2021

	March 31, 2022	March 31, 2021
Cash Flows from Operating Activities:		
Net income (loss)	\$ 988,621	\$ (1,061,297)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Stock-based compensation	134,266	106,286
Depreciation	373,830	399,197
ESOP compensation expense	245,362	218,750
Gain on disposal of assets	(2,000)	—
Deferred income tax benefit	(50,336)	(53,873)
Changes in assets and liabilities:		
(Increase) decrease in trade accounts receivable	(289,088)	6,755,964
Decrease (increase) in income taxes receivable	158,439	(168,201)
Increase in inventories	(152,211)	(4,474,719)
Increase in prepaid expenses and other current assets	(228,539)	(55,565)
Decrease in accounts payable	(619,925)	(1,531)
Increase (decrease) in accrued salaries and wages	101,487	(117,859)
Increase in vacation accrual	79,846	83,430
Decrease in ESOP Payable	—	(75,000)
Increase (decrease) in other accrued expenses	145,789	(160,678)
(Decrease) increase in payroll and other taxes withheld	(350,924)	278,375
Increase in contract liabilities	276,461	562,728
Decrease in income taxes payable	—	(47,707)
Net cash provided by operating activities	811,078	2,188,300
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(216,500)	(34,337)
Proceeds from sale of fixed assets	2,000	—
Purchase of investment securities	(3,692,458)	(4,294,897)
Proceeds from sale/maturity of investment securities	3,576,000	6,429,064
Net cash (used in) provided by investing activities	(330,958)	2,099,830
Cash Flows from Financing Activities:		
Dividends on common stock	—	(1,201,316)
Net cash used in financing activities	—	(1,201,316)
Increase in cash and cash equivalents	480,120	3,086,814
Cash and cash equivalents, beginning of period	6,802,712	5,402,122
Cash and cash equivalents, end of period	\$ 7,282,832	\$ 8,488,936
Supplemental Schedule of Cash Flow Information:		
Income taxes paid	\$ 120,000	\$ 175,250

The accompanying notes are an integral part of the financial statements.

ESPEY MFG. & ELECTRONICS CORP.
Notes to Financial Statements (Unaudited)

Note 1. Basis of Presentation

In the opinion of management the accompanying unaudited financial statements contain all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the results for such periods. The results for any interim period are not necessarily indicative of the results to be expected for the full fiscal year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with United States generally accepted accounting principles have been condensed or omitted. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of assets and liabilities. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenue recognition, inventories, income taxes, and stock-based compensation. Specific to inventories, including work-in-process and contracts in process, management evaluates, quarterly, those estimates used in determining the cost to complete for each contract on Espey Mfg. & Electronics Corp. (the "Company") sales backlog. The change in estimates may affect the reported amount of inventories and gross profit in the current or a future period. Management bases its estimates on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. These financial statements should be read in conjunction with the Company's most recent audited financial statements included in its report on Form 10-K for the year ended June 30, 2021. Certain reclassifications may have been made to the prior year financial statements to conform to the current year presentation.

Note 2. Investment Securities

Accounting Standards Codification ("ASC") 820 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
- Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The carrying amounts of financial instruments, including cash and cash equivalents, short term investments, accounts receivable, accounts payable and accrued expenses, approximated fair value as of March 31, 2022 and June 30, 2021 because of the immediate or short-term maturity of these financial instruments.

Investment securities at March 31, 2022 consists of certificates of deposit and municipal bonds and at June 30, 2021 consisted of certificates of deposit. The Company classifies investment securities as available-for-sale which have been determined to be level 1 assets. The cost, gross unrealized gains, gross unrealized losses and fair value of available-for-sale securities by major security type at March 31, 2022 and June 30, 2021 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<u>March 31, 2022</u>				
Certificates of deposit	\$ 3,139,000	\$ —	\$ —	\$ 3,139,000
Municipal bonds	\$ 72,225	\$ —	\$ (1,928)	\$ 70,297
Total investment securities	\$ 3,211,225	\$ —	\$ (1,928)	\$ 3,209,297
<u>June 30, 2021</u>				
Certificates of deposit	\$ 3,092,000	\$ —	\$ —	\$ 3,092,000

The portfolio is diversified and highly liquid and primarily consists of investment grade fixed income instruments. At March 31, 2022, the Company did not have any investments in individual securities that have been in a continuous loss position considered to be other than temporary.

As of March 31, 2022 and June 30, 2021, the remaining contractual maturities of available-for-sale securities were as follows:

	Years to Maturity		Total
	Less than One Year	One to Five Years	
<u>March 31, 2022</u>			
Available-for-sale	\$ <u>3,209,297</u>	\$ —	\$ <u>3,209,297</u>
<u>June 30, 2021</u>			
Available-for-sale	\$ <u>3,092,000</u>	\$ —	\$ <u>3,092,000</u>

Note 3. Net Income (Loss) per Share

Basic net income (loss) per share excludes dilution and is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted net income (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 or resulted in the issuance of common stock that then shared in the income of the Company. The computation of diluted net income per share, excluded options to purchase 264,978 shares of our common stock for the three and nine months ended March 31, 2022 and the computation of diluted net loss per share, excluded options to purchase 312,187 shares for the three and nine months ended March 31, 2021, as the effect of including them would be anti-dilutive. As unearned shares owned by the Company's sponsored leveraged employee stock ownership plan (the "ESOP") are released or committed-to-be-released, the shares become outstanding for earnings-per-share computations.

Note 4. Stock Based Compensation

The Company follows ASC 718 in establishing standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, as well as transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. ASC 718 requires that the cost resulting from all share-based payment transactions be recognized in the financial statements based on the fair value of the share-based payment. ASC 718 establishes fair value as the measurement objective in accounting for share-based payment transactions with employees, except for equity instruments held by employee share ownership plans.

Total stock-based compensation expense recognized in the statements of comprehensive income (loss) for the three-month periods ended March 31, 2022 and 2021 was \$39,699 and \$25,412, respectively, before income taxes. The amount of this stock-based compensation expense related to non-qualified stock options ("NQSO") for the three-month periods ended March 31, 2022 and 2021, was \$6,582 and \$7,366, respectively. The deferred tax benefit related to the NQSO's as of March 31, 2022 and 2021 was approximately \$1,382 and \$1,547, respectively. Total stock-based compensation expense recognized in the statements of comprehensive income (loss) for the nine-month periods ended March 31, 2022 and 2021, was \$134,266 and \$106,286, respectively, before income taxes. The amount of this stock-based compensation expense related to non-qualified stock options ("NQSO") for the nine-month periods ended March 31, 2022 and 2021, was \$22,705 and \$25,497, respectively. The deferred tax benefit related to the NQSO's as of March 31, 2022 and 2021 was approximately \$4,768 and \$5,354, respectively. The remaining stock option expense in each year related to incentive stock options ("ISO") which are not deductible by the corporation when exercised, assuming a qualifying disposition and as such no deferred tax benefit was established related to these amounts.

As of March 31, 2022, there was approximately \$179,612 of unrecognized compensation cost related to stock option awards that is expected to be recognized as expense over the next 1.75 years, of which \$146,291 relates to ISO's and \$33,321 relates to NQSO's. The total deferred tax benefit related to these non-qualified stock option awards is expected to be \$6,997.

The Company has one employee stock option plan under which options or stock awards may be granted, the 2017 Stock Option and Restricted Stock Plan (the "2017 Plan"). The Board of Directors may grant options to acquire shares of common stock to employees and non-employee directors of the Company at the fair market value of the common stock on the date of grant. The maximum aggregate number of shares of Common Stock subject to options or awards to non-employee directors is 133,000 and the maximum aggregate number of shares of Common Stock subject to options or awards granted to non-employee directors during any single fiscal year is the lesser of 13,300 and 33 1/3% of the total number of shares subject to options or awards granted in such fiscal year. The maximum number of shares subject to options or awards granted to any individual employee may not exceed 15,000 in a fiscal year. Generally, options granted have a two-year vesting period based on two years of continuous service and have a ten-year contractual life. Option grants provide for accelerated vesting if there is a change in control. The plan allows for cancelled or expired options to be re-granted to participants at a later date. Shares issued upon the exercise of options are from those held in Treasury. Options covering 400,000 shares are authorized for issuance under the 2017 Plan. As of March 31, 2022, options covering 303,904 shares have been granted, of which 198,578 are outstanding, and 201,422 remain available for grant, after factoring cancelled or expired options which are eligible to be re-granted. While no further grants of options may be made under the Company's 2007 Stock Option and Restricted Stock Plan, as of March 31, 2022, 66,400 options were outstanding under such plan of which all are vested and exercisable.

ASC 718 requires the use of a valuation model to calculate the fair value of stock-based awards. The Company has elected to use the Black-Scholes option valuation model, which incorporates various assumptions including those for dividend yield, volatility, expected life and interest rates.

The table below outlines the weighted average assumptions that the Company used to calculate the fair value of each option award for the nine months ended March 31, 2022 and 2021.

	<u>March 31, 2022</u>	<u>March 31, 2021</u>
Dividend yield	<u>0%</u>	<u>5.54%</u>
Company's expected volatility	<u>25.56%</u>	<u>23.41%</u>
Risk-free interest rate	<u>0.93%</u>	<u>0.36%</u>
Expected term	<u>5.4 yrs</u>	<u>5.4 yrs</u>
Weighted average fair value per share of options granted during the period	<u>\$3.72</u>	<u>\$1.59</u>

Effective March 9, 2021, the Company suspended the payment of its regular quarterly dividend. For the nine months ended March 31, 2022, the Company paid no cash dividends. For the nine months ended March 31, 2021, the Company paid regular cash dividends of \$0.50 per share. Expected stock price volatility is based on the historical volatility of the Company's stock. The risk-free interest rate is based on the implied yield available on U.S. Treasury issues with an equivalent term approximating the expected life of the options. The expected option term (in years) represents the estimated period of time until exercise and is based on actual historical experience.

The following table summarizes stock option activity during the nine months ended March 31, 2022:

	<u>Employee Stock Options Plan</u>			
	<u>Number of Shares Subject to Option</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
Balance at July 1, 2021	<u>304,662</u>	<u>\$ 23.37</u>	<u>6.06</u>	
Granted	<u>77,550</u>	<u>\$ 14.76</u>	<u>9.31</u>	
Exercised	<u>—</u>	<u>—</u>	<u>—</u>	
Forfeited or expired	<u>(117,234)</u>	<u>\$ 22.62</u>	<u>—</u>	
Outstanding at March 31, 2022	<u>264,978</u>	<u>\$ 21.18</u>	<u>6.57</u>	<u>\$ --</u>
Vested or expected to vest at March 31, 2022	<u>246,809</u>	<u>\$ 21.56</u>	<u>6.40</u>	<u>\$ --</u>
Exercisable at March 31, 2022	<u>160,953</u>	<u>\$ 24.51</u>	<u>4.99</u>	<u>\$ --</u>

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (the difference between the closing sale price of the Company's common stock as reported on the NYSE American on March 31, 2022 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders if all option holders had exercised their options on March 31, 2022. This amount changes based on the fair market value of the Company's common stock. The intrinsic value of options exercised during the nine months ended March 31, 2022 and 2021 was \$0, resulting from no option exercise activity during those periods.

The following table summarizes changes in non-vested stock options during the nine months ended March 31, 2022:

	Weighted Number of Shares Subject to Option	Average Grant Date Fair Value (per Option)
Non-vested at July 1, 2021	<u>103,450</u>	\$ <u>2.22</u>
Granted	<u>77,550</u>	\$ <u>3.72</u>
Vested	<u>(43,025)</u>	\$ <u>3.03</u>
Forfeited or expired	<u>(33,950)</u>	\$ <u>2.55</u>
Non-vested at March 31, 2022	<u>104,025</u>	\$ <u>2.90</u>

Note 5. Commitments and Contingencies

The Company from time to time, enters into standby letters of credit agreements with financial institutions primarily relating to the guarantee of future performance on certain contracts. Contingent liabilities on outstanding standby letters of credit agreements aggregated to zero at March 31, 2022 and June 30, 2021. The Company, as a U.S. Government contractor, is subject to audits, reviews, and investigations by the U.S. Government related to its negotiation and performance of government contracts and its accounting for such contracts. Failure to comply with applicable U.S. Government standards by a contractor may result in suspension from eligibility for award of any new government contract and a guilty plea or conviction may result in debarment from eligibility for awards. The government may, in certain cases, also terminate existing contracts, recover damages, and impose other sanctions and penalties. As a result of contract audits the Company will determine a range of possible outcomes and in accordance with ASC 450 "Contingencies" the Company will accrue amounts within a range that appears to be its best estimate of a possible outcome. Adjustments are made to accruals, if any, periodically based on current information.

We are party to various litigation matters and claims arising from time to time in the ordinary course of business. There are no such pending matters which we believe will have a material adverse effect on our business, financial condition, results of operations or cash flows.

Note 6. Revenue

The Company follows ASC 606 "Revenue from Contracts with Customers" to determine the recognition of revenue. This standard requires entities to assess the products or services promised in contracts with customers at contract inception to determine the appropriate unit at which to record revenues. Revenue is recognized when control of the promised products or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those products or services.

Significant judgment is required in determining the satisfaction of performance obligations. Revenues from our performance obligations are satisfied over time using the output method which considers the appraisal of results achieved and milestones reached or units delivered based on contractual shipment terms, typically shipping point. Revenue is recognized when, or as, the customer takes control of the product or services. The output method best depicts the transfer of control to the customer as the output method represents work completed. Control is typically transferred to the customer at the shipping point as the Company has a present right to payment, the customer has legal title to the asset, the customer has the significant risks and rewards of ownership of the asset, and in most instances the customer has accepted the asset.

Total revenue recognized for the three and nine months ended March 31, 2022 based on units delivered was \$7,291,109 and \$19,883,573, respectively, compared to \$3,754,628 and \$15,479,212 for the same periods in fiscal year 2021. Total revenue recognized for the three and nine months ended March 31, 2022 based on milestones achieved was \$1,328,940 and \$3,739,958, respectively, compared to \$450,440 and \$2,953,436 for the same periods in fiscal year 2021.

The Company offers a standard one-year product warranty. Product warranties offered by the Company are classified as assurance-type warranties, which means, the warranty only guarantees that the good or service functions as promised. Based on this, the provided warranty is not considered to be a distinct performance obligation. The impact of variable consideration has been considered but none identified which would be required to be allocated to the transaction price as of March 31, 2022. Our payment terms are generally 30-60 days.

Contract liabilities were \$3,354,066 and \$3,077,605 as of March 31, 2022 and June 30, 2021, respectively. The increase in contract liabilities is primarily due to the advance collection of cash on specific contracts, offset in part, by revenue recognized. Revenue recognized, that was in contract liabilities in the beginning of the fiscal year, approximated \$811,000 for the nine months ended March 31, 2022. The Company used the practical expedient to expense incremental costs incurred to obtain a contract when the contract term is less than one year.

The Company's backlog at March 31, 2022 totaling approximately \$76.2 million is projected, based on expected due dates, to be recognized in the following fiscal years: 13% in 2022; 48% in 2023; 29% in 2024, and 10% thereafter.

Note 7. Recently Issued Accounting Standards

Recent Accounting Pronouncements Adopted

In December 2019, the FASB issued ASU 2019-12, "Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes." ASU 2019-12 amends ASC 740 to simplify the accounting for income taxes by removing certain exceptions for investments, intraperiod allocations and interim calculations, and adding guidance to reduce complexity in the accounting standard under the FASB's simplification initiative. ASU 2019-12 is effective for public entities for fiscal years beginning after December 15, 2020. Upon adoption, the amendments in ASU 2019-12 should be applied on a prospective basis to all periods presented. The Company adopted the new guidance under ASU 2019-12 in the first quarter of fiscal year 2021 and removed the exception for intraperiod allocations from its interim period tax provision calculation, accordingly. The removal of the exception for intraperiod allocations did not have a material impact on the Company.

Note 8. Employee Stock Ownership Plan

The Company sponsors a leveraged employee stock ownership plan (the "ESOP") that covers all nonunion employees who work 1,000 or more hours per year and are employed on June 30. Prior to December 1, 2020, the ESOP owned 469,119 shares, all of which were allocated to employees. On December 1, 2020, pursuant to a Stock Purchase Agreement dated as of such date, the Company, by selling 300,000 shares of its common stock, par value \$0.33 1/3 per share, to the Espey Mfg. & Electronics Corp. Employee Stock Ownership Plan Trust, provided more shares to be allocated to employees for services rendered over the next 15 years. The ESOP paid \$18.29 per share, for an aggregate purchase price of \$5,487,000. The determination of the purchase price was based on a fairness opinion obtained by an independent valuation firm. The ESOP borrowed from the Corporation an amount equal to the purchase price. The loan will be repaid in fifteen (15) equal annual installments of principal. The Board of Directors has fixed the interest rate and the unpaid balance will bear interest at a fixed rate of 3.00% per annum.

The Board of Directors of the Company had approved a purchase price per share equal to the lesser of the trading value on the day of closing or the lowest price listed in the valuation established by the independent valuation firm plus \$0.25. The valuation identified a range of \$18.04 - \$19.43 per share.

In making the sale, the Company relied on the exemption from registration under Section 4(2) of the Securities Act of 1933, as amended, because the shares sold were offered only to the ESOP.

After giving effect to the transaction, the ESOP owned 769,119 shares of the Company's 2,702,633 outstanding shares of common stock as of December 1, 2020.

The Company makes annual contributions to the ESOP equal to the ESOP's debt service less dividends on unallocated shares received by the ESOP. Any dividends on unallocated shares received by the ESOP are used to pay debt service. Any dividends on allocated ESOP shares are recorded as a reduction of retained earnings. As the debt is repaid, shares are released and allocated to active employees, based on the proportion of debt service paid in the year. The Company accounts for its ESOP in accordance with FASB ASC 718-40. Accordingly, the shares purchased by the ESOP are reported as Unearned ESOP shares in the balance sheets and the statements of changes in stockholders' equity. As shares are released or committed-to-be-released, the Company reports compensation expense equal to the current average market price of the shares, and the shares become outstanding for earnings-per-share (EPS) computations. ESOP compensation expense was \$77,045 and \$162,476 for the three-month periods ended March 31, 2022 and 2021, respectively. ESOP compensation expense was \$245,362 and \$218,750 for the nine-month periods ended March 31, 2022 and 2021, respectively.

The ESOP shares as of March 31, 2022 and 2021 were as follows:

	March 31, 2022	March 31, 2021
Allocated shares	<u>472,955</u>	<u>467,104</u>
Committed-to-be-released shares	<u>17,352</u>	<u>11,755</u>
Unreleased shares	<u>262,077</u>	<u>288,245</u>
Total shares held by the ESOP	<u>752,384</u>	<u>767,104</u>
Fair value of unreleased shares	<u>\$ 3,642,870</u>	<u>\$ 4,381,324</u>

The Company may at times be required to repurchase shares at the ESOP participants' request at the shares' fair market value. During the three and nine months ended March 31, 2022 and 2021, the Company did not repurchase shares previously held by the ESOP.

The ESOP allows for eligible participants to take whole share distributions from the Plan on specific dates in accordance with the provision of the Plan. Share distributions from the ESOP during the nine months ended March 31, 2022 and 2021 totaled 14,265 and 2,015 shares, respectively.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Espey Mfg. & Electronics Corp. ("Espey") is a power electronics design and original equipment manufacturing (OEM) company with a long history of developing and delivering highly reliable products for use in military and severe environment applications. Design, manufacturing, and testing is performed in our 150,000+ square foot facility located at 233 Ballston Ave, Saratoga Springs, New York. Espey is classified as a "smaller reporting company" for purposes of the reporting requirements under the Securities Exchange Act of 1934, as amended. Espey's common stock is publicly-traded on the NYSE American under the symbol "ESP."

Espey began operations after incorporation in New York in 1928. We strive to remain competitive as a leader in high power energy conversion and transformer solutions through the design and manufacture of new and improved products by using advanced and "cutting edge" electronics technologies.

Espey is ISO 9001:2015 and AS9100:2016 certified. Our primary products are power supplies, power converters, filters, power transformers, magnetic components, power distribution equipment, UPS systems, antennas and high power radar systems. The applications of these products include AC and DC locomotives, shipboard power, shipboard radar, airborne power, ground-based radar, and ground mobile power.

Espey services include design and development to specification, build to print, design services, design studies, environmental testing services, metal fabrication, painting services, and development of automatic testing equipment. Espey is vertically integrated, meaning that the Company produces individual components (including inductors), populates printed circuit boards, fabricates metalwork, paints, wires, qualifies, and fully tests items, mechanically, electrically and environmentally, in house. Portions of the manufacturing and testing process are subcontracted to vendors from time to time.

The Company markets its products primarily through its own direct sales organization and through outside sales representatives. Business is solicited from large industrial manufacturers and defense companies, the government of the United States, foreign governments and major foreign electronic equipment companies. Espey is also on the eligible list of contractors with the United States Department of Defense. We pursue opportunities for prime contracts directly with the Department of Defense and are generally automatically solicited by Department of Defense procurement agencies for their needs falling within the major classes of products produced by the Company. Espey contracts with the Federal Government under cage code 20950 as Espey Mfg. & Electronics Corp.

There is competition in all classes of products manufactured by the Company, ranging from divisions of the largest electronic companies, to many small companies. The Company's sales do not represent a significant share of the industry's market for any class of its products. The principal methods of competition for electronic products of both a military and industrial nature include, among other factors, price, product performance, the experience of the particular company and history of its dealings in such products.

Our business is not seasonal. However, the concentration of our business in the rail industry, and in equipment for military applications and industrial applications, and our customer concentrations expose us to on-going associated risks. These risks include, without limitation, fluctuating requirements for power supplies in the rail industry, dependence on appropriations from the United States Government and the governments of foreign nations, program allocations, the potential of governmental termination of orders for convenience, and the general strength of the industry sectors in which our customers transact business.

Future procurement needs supporting the military and the rail industry continue to drive competition. Many of our competitors have invested, and they continue to invest aggressively in upfront product design costs and accept lower profit margins as a strategic means of maintaining existing business and enhancing market share. This continues to put pressure on the pricing of our current products and has lowered our profit margins on some of our new business. In order to compete effectively for new business, in some cases we have invested in upfront design costs, thereby reducing initial profitability as a means of procuring new long-term programs. As part of our strategy, we adjust our pricing in order to achieve a balance which enables us both to retain repeat programs while being more competitive in bidding on new programs.

[Index](#)

We continue to place an emphasis on securing “build to print” opportunities, which will allow production work to go directly to the manufacturing floor, limiting the impact on our engineering staff. This allows us to keep our manufacturing team busy while the products are being developed in-house to production.

The total backlog at March 31, 2022 was approximately \$76.2 million, which included \$47.5 million from four significant customers, compared to approximately \$67.3 million at March 31, 2021, which included \$43.6 million from five significant customers. The Company’s total backlog represents the estimated remaining sales value of work to be performed under firm contracts. The funded portion of this backlog at March 31, 2022 is approximately \$75.8 million. This includes items that have been authorized and appropriated by Congress and/or funded by the customer. The unfunded backlog at March 31, 2022 is approximately \$0.4 million and represents two firm multi-year orders from a single customer for which funding has not yet been appropriated by Congress or funded by our customer. While there is no guarantee that future budgets and appropriations will provide funding for individual programs, management has included in unfunded backlog only those programs that it believes are likely to receive funding based on discussions with customers and program status. The unfunded backlog at March 31, 2021 was approximately \$2.1 million, comprised of the same multi-year orders from a single customer. Contracts are subject to modification, change or cancellation, and the Company accounts for these changes as they are probable and estimable. The Company evaluates the impact of any scope modifications and will adjust reserves as information is known and estimable.

Successful conversion of engineering program backlog into sales is largely dependent on the execution and completion of our engineering design efforts. It is not uncommon to experience technical or scheduling delays which arise from time to time as a result of, among other reasons, design complexity, the availability of personnel with the requisite expertise, and the requirements to obtain customer approval at various milestones. Cost overruns which may arise from technical and schedule delays could negatively impact the timing of the conversion of backlog into sales, or the profitability of such sales. We continue to experience technical and schedule delays with our major development programs. To date, we have been able to resolve various technical and scheduling delays and continue to work with our customers on newly arising delays. Engineering programs in both the funded and unfunded portions of the current backlog aggregate \$7.2 million.

The growth and continuing demand in the power electronics industry across multiple manufacturing sectors has created volatility and unpredictability in the availability of certain electronic components and, in some cases, continues to create industry shortages. These shortages have and will likely continue to impact our ability to support our customer’s schedule demands, as lead times for these components have, in some instances, increased from readily available to waiting times of nearly a year or more. In addition, we continue to incur delays in material deliveries from some company suppliers due to the COVID-19 pandemic.

Effects from global events and the resulting supply chain disruptions continue to place pressure on the cost of raw materials, freight, utility, labor and other production and administrative costs. These inflationary cost challenges are expected to continue to have a negative impact on operating income in the near term. Volatile raw material indexes and shortages have led to wide-spread vendor price increases. In turn, pricing extended to our customers, through product quotations, has increased, and in some instances significantly, reflective of this unstable inflationary market. In addition, as we navigate through these challenges, we have reduced the time in which certain product quotations remain valid and have also extended lead times, in many instances. As for our executed fixed-priced contracts, we will either singularly or combined be 1) required to absorb the increased costs 2) continue to mitigate costs down through the identification of additional supply chain buying strategies or 3) seek price remediation assistance from our customers. We continue to work with our customers to mitigate any adverse impact upon our ability to service their requirements.

Management continues to closely monitor the impact of evolving workforce labor constraints, primarily from the effects from the pandemic, on our planned delivery schedules. Although declining, we continue to experience periodic disruptions from workforce absences due to COVID-19 illnesses and direct contact exposures, resulting in self-isolating protocols to be followed to ensure the safety of company personnel. Disruptions from workforce turnover resulting from a competitive employee market still occurs, however at a decreased rate, having stabilized in the last three months. Several key positions still remain open. Combined, with supply chain constraints, these ongoing labor disruptions may delay shipments and result in recognizing lower operating income.

Management expects revenues in fiscal year 2022 to be higher than revenues during fiscal year 2021 and expects to generate net income per share as compared to the net loss per share realized during fiscal year 2021. These expectations are driven by orders already in our sales backlog. Creating consistency in our quarter to quarter financial performance will remain a challenge as we move forward navigating this difficult environment of inflation and part shortages.

[Index](#)

The Company currently expects new orders in fiscal 2022 to approximate the \$38.5 million in new orders received in fiscal year 2021. As market factors including competition and product costs impact gross profit margins, management will continue to evaluate our sales strategy, employment levels, and facility costs.

New orders received in the first nine months of fiscal year 2022 were \$34.1 million as compared to \$30.8 million new orders received in the first nine months of fiscal 2021. It is presently anticipated that a minimum of \$10 million of orders comprising the March 31, 2022 backlog will be filled during the fiscal year ending June 30, 2022 subject, however, to the impact of the factors identified above. The minimum of \$10 million does not include any shipments, which may be made against orders subsequently received during the fiscal year ending June 30, 2022.

In addition to the backlog, the Company currently has outstanding opportunities representing approximately \$62 million in the aggregate as of May 11, 2022 for both repeat and new programs. The outstanding quotations encompass various new and previously manufactured power supplies, transformers, and subassemblies. However, there can be no assurance that the Company will acquire any of the anticipated orders described above, many of which are subject to allocations of the United States defense spending and factors affecting the defense industry.

A significant portion of the Company's business is the production of military and industrial electronic equipment for use by the U.S. and foreign governments and certain industrial customers. Net sales to four significant customers represented approximately 61% of the Company's total sales for the three-month period ended March 31, 2022. Net sales to five significant customers represented 66% of the Company's total sales for the three-month period ended March 31, 2021. Net sales to four significant customer represented approximately 55% of the Company's total sales for the nine-month period ended March 31, 2022. Net sales to four significant customers represented 57% of the Company's total sales for the nine-month period ended March 31, 2021. A loss of one of these customers or programs related to these customers, or customer requested deferrals of product delivery could significantly impact the Company.

Historically, a small number of customers have accounted for a large percentage of the Company's total sales in any given fiscal year. Management continues to pursue opportunities with current and new customers with an overall objective of lowering the concentration of sales, mitigating excessive reliance upon a single major product of a particular program and minimizing the impact of the loss of a single significant customer. Given the nature of our business, we believe our existing sales order backlog is fairly diversified in terms of customers and the category of products on order.

Critical Accounting Policies and Estimates

Management believes our most critical accounting policies include revenue recognition and cost estimation on our contracts.

Revenue

The majority of our net sales is generated from contracts with industrial manufacturers and defense companies, the Department of Defense, other agencies of the government of the United States and foreign governments for the design, development and/or manufacture of products. We provide our products and design and development services under fixed-price contracts. Under fixed-price contracts we agree to perform the specified work for a pre-determined price. To the extent our actual costs vary from the estimates upon which the price was negotiated, we will generate more or less profit or could incur a loss.

We account for a contract after it has been approved by all parties to the arrangement, the rights of the parties are identified, payment terms are identified, the contract has commercial substance, and collectability of consideration is probable. We assess each contract at its inception to determine whether it should be combined with other contracts. When making this determination, we consider factors such as whether two or more contracts were negotiated and executed at or near the same time, or were negotiated with an overall profit objective.

We evaluate the products or services promised in each contract at inception to determine whether the contract should be accounted for as having one or more performance obligations. Significant judgment is required in determining performance obligations. We determine the transaction price for each contract based on the consideration we expect to receive for the products or services being provided under the contract. The transaction price for each performance obligation is based on the estimated standalone selling price of the product or service underlying each performance obligation. Transaction prices on our contracts subject to the Federal Acquisition Regulations (FAR) are typically based on estimated costs plus a reasonable profit margin.

[Index](#)

We recognize revenue using the output method based on the appraisal of results achieved and milestones reached or units delivered based on contractual shipment terms, typically shipping point.

Inventory

Raw materials are valued at the lower of cost (average cost) or net realizable value. Balances for slow-moving and obsolete inventory are reviewed on a regular basis by analyzing estimated demand, inventory on hand, sales levels, market conditions, and other information and reduce inventory balances based on this analysis.

Inventoried work relating to contracts in process and work in process is valued at actual production cost, including factory overhead incurred to date. Contract costs include material, subcontract costs, labor, and an allocation of overhead costs. Work in process represents spare units and parts and other inventory items acquired or produced to service units previously sold or to meet anticipated future orders. Provision for losses on contracts is made when the existence of such losses becomes probable and estimable. The provision for losses on contracts is included in other accrued expenses on the Company's balance sheet. The costs attributed to units delivered under contracts are based on the estimated average cost of all units expected to be produced. Certain contracts are expected to extend beyond twelve months.

The estimation of total cost at completion of a contract is subject to numerous variables involving contract costs and estimates as to the length of time to complete the contract. Given the significance of the estimation processes and judgments described above, it is possible that materially different amounts of expected sales and contract costs could be recorded if different assumptions were used, based on changes in circumstances, in the estimation process. When a change in expected sales value or estimated cost is determined, the change is reflected in current period earnings.

Contract Liabilities

Contract liabilities include advance payments and billings in excess of revenue recognized.

Results of Operations

Net sales increased for the three months ended March 31, 2022 to \$8,620,049 as compared to \$4,205,068 for the same period in 2021. Net sales for the nine months ended March 31, 2022 increased to \$23,623,531 as compared to \$18,432,648 for the same period in 2021. For the three months ended March 31, 2022, sales increased primarily from an increase in power supply and magnetic shipments. For the nine months ended March 31, 2022, the increase in sales is primarily due to an increase in magnetic, power supply, and build to print sales. In general, sales fluctuations within product categories will occur during a comparable fiscal period as the direct result of product mix, influenced by the duration of specific programs and the contractual terms of firm orders placed for product and services under those programs including contract value, scope of work and duration. Deliverables within firm contracts are often subject to delivery schedules which also contributes to sales fluctuations between comparable periods. Internal and external constraints, at times, impact our ability to ship.

The impact of ongoing global events, most notably the COVID-19 pandemic, continues to drive instability in our supply chain. Unplanned employee absences due to sickness and self-isolating protocols continues, but have been significantly less compared to a year ago. Disruptions from workforce turnover resulting from a competitive employee market continues, but have begun to subside in the last three months. However, combined, these ongoing factors continue to constrain our ability to ship product to our customers.

Specific to the current three and nine month periods discussed above, the sales fluctuations when compared to the same periods last year were primarily the direct result of an unplanned facility closure which occurred in March 2021 due to a significant workforce COVID-19 exposure. The closure lasted approximately 10 days with the facility re-opening at less than full capacity. In addition, the increase in sales in the current fiscal year was influenced by product mix, contractual due dates, and our ability to deliver on certain past due customer orders which had been delayed due to extended raw material lead times. Finally, sales were favorably impacted by the completion of certain engineering milestones.

[Index](#)

In addition, our operations continue to be adversely impeded by (i) engineering design changes required to meet customer requirements, (ii) certain supplier product non-conformances, (iii) delays in obtaining timely resolutions on issues encompassing build to print customer-owned drawings, and (iv) an increase in lead times for many parts, including certain electronic components due to industry shortages and volatility within the power electronics industry. Engineering, program management, and supply chain personnel are working closely with our customers and suppliers to execute on our past due deliveries and we do not expect this situation to affect future business opportunities.

Gross profit (loss) for the three months ended March 31, 2022 and 2021 was \$1,734,880 and \$(187,154), respectively. Gross profit (loss) as a percentage of sales was approximately 20.1% and (4.5)%, for the same periods, respectively. For the nine months ended March 31, 2022 and 2021, gross profits were \$4,294,795 and \$1,653,681, respectively. Gross profit as a percentage of sales was 18.2% and 9.0%, for the same periods, respectively. The primary factors in determining the change in gross profit and net income are overall sales levels and product mix. The gross profits on mature products and build to print contracts are typically higher as compared to products which are still in the engineering development stage or in early stages of production. In the case of the latter, the Company can incur what it refers to as "loss contracts," primarily on engineering design contracts in which the Company invests with the objective of developing future product sales. In any given accounting period the mix of product shipments between higher margin programs and less mature programs, and expenditures associated with loss contracts, has a significant impact on gross profit and net income.

Many factors added to an increase in gross profit in the three months ended March 31, 2022 as compared to the same period in 2021. Comparatively, there were several events which occurred in the comparable period last year contributing to the recognized gross loss, which did not have a negative impact on gross profit in the current fiscal quarter. First, lower sales resulting from the unplanned facility shutdown due to the COVID-19 pandemic, had a significant impact on gross profit recognized during the three months ended March 31, 2021. Second, also attributable to the pandemic, the Company wrote down the remaining value of inventory pertaining to a certain design and production contract serving the airline industry which was cancelled by the customer during the second quarter of the prior fiscal year, and with respect to which the Company was unsuccessful in being awarded restitution. Finally, the Company had recognized increased costs on two specific engineering design and production contracts, which negatively impacted gross profit last year, while accounting for higher sales and contributing to gross profit in the current quarter due to lower than expected labor costs on certain milestones and production costs required for those contracts. Specific to the current fiscal quarter, the Company recognized higher gross profit related to higher sales on mature power supply and from build to print shipments when compared to the same period last year. These improvements to gross profit were offset, in part, by an unforeseen significant increase in material costs on a large production contract, a direct result of inflationary and volatile pricing for certain raw materials and components. The Company is reviewing opportunities with the customer concerning potential equitable adjustments to this long-term fixed price contract supporting the US military.

The improvement in gross profit in the nine months ended March 31, 2022 as compared to the same period in 2021 resulted from an increase in power supply, magnetic and build to print shipments and product mix comprising those shipments. In addition, similar to the three month results discussed above, gross profit for the nine month period improved when compared to the prior year as specific items which negatively impacted prior year results did not have a negative impact on gross profit recognized in the current year. Reductions to gross profit in the prior year included lower sales as the result of an unplanned facility shutdown in the third quarter of last year, and the costs incurred for an inventory write-down for a design and production contract serving the airline industry, which was cancelled by the customer during the second quarter of the prior fiscal year. Two specific engineering design and production contracts, which due to increased costs had a negative impact on gross profit last year, had higher sales in the current fiscal year and contributed to gross profit. In addition, the Company recognized higher gross profit on increased sales on mature power supply programs and from build to print shipments when compared to the same period last year. These improvements to gross profit were offset, in part, by increased costs incurred on a power supply engineering design and production contract when compared to the prior year. Finally, gross profit was reduced by a large increase in unforeseen material cost escalations on a large production contract during the current quarter of fiscal 2022, a direct result of the inflationary and volatile pricing for certain raw materials and components.

Selling, general and administrative expenses were \$933,725 for the three months ended March 31, 2022, a decrease of \$56,586, compared to the three months ended March 31, 2021. Selling, general and administrative expenses were \$3,114,715 for the nine months ended March 31, 2022, an increase of \$264,300 compared to the nine months ended March 31, 2021. The decrease for the three months ended March 31, 2022 as compared to the same period in 2021 relates primarily to the decrease in employee compensation costs due to a reduction in headcount and position vacancies, a decrease in cost associated with scheduled allocated shares from the leveraged ESOP and the decrease in board of director's fees due to a reduction of two non-employee directors. These decreases were offset, in part, by an increase in costs incurred to recruit and fill company-wide position vacancies, travel, conferences and training, utility expenses and freight costs. The increase for the nine months ended March 31, 2022 as compared to the same period in 2021 resulted primarily from the costs recorded in the second quarter of the current fiscal year as the result of a change in senior management, an increase in costs incurred to recruit and fill company-wide position vacancies, an increase in professional services due to timing of progress billings, and increase in conferences and training, travel costs, and an increase in utility expenses. These increases were offset, in part, by a decrease in employee compensation costs due to a reduction in headcount and position vacancies and a decrease in board of director's fees due to a reduction of two non-employee directors.

[Index](#)

Other income for the three months ended March 31, 2022 and 2021 was \$5,661 and \$7,075, respectively. Other income for the nine months ended March 31, 2022 and 2021 was \$37,049 and \$40,906, respectively. The decrease for the three months ended March 31, 2022 as compared to the same period in 2021 is primarily due to the decrease in other income primarily comprised of income from scrap sales, offset, in part, by an increase in income on the sale of a fixed asset. The decrease for the nine months ended March 31, 2022 as compared to the same period in 2021 is primarily due to a decrease in interest income, resulting from updated investment strategies which yield lower interest while maintaining higher liquidity, offset, in part, by an increase in other income primarily comprised of income from scrap sales. Interest income is a function of the level of investments and investment strategies that generally tend to be conservative.

The Company's effective tax rate for the three and nine months ended March 31, 2022 was approximately 18.0% and 18.8%, respectively, compared to 8.6% and 8.2% for the three and nine months ended March 31, 2021. The effective tax rate in fiscal 2022 and 2021 is less than the statutory tax rate mainly due to the benefit derived from the ESOP dividends paid on allocated shares. The effective tax rate in the three and nine month periods ended March 31, 2022 was higher than the prior year as the direct result of a higher income before taxes in the current fiscal year offset, in part, by a decreased benefit derived from ESOP dividends paid on allocated shares.

Net income for the three months ended March 31, 2022, was \$661,359 or \$0.27 per share, basic and diluted, compared to net loss of \$(1,070,114) or \$(0.44) per share, basic and diluted, for the three months ended March 31, 2021. Net income for the nine months ended March 31, 2022 was \$988,621 or \$0.41 per share, basic and diluted, compared to net loss of \$(1,061,297) or \$(0.44) per share, basic and diluted, for the nine months ended March 31, 2021. The increase in net income in the three months ended resulted from the increase in gross profit and the decrease in selling, general and administrative expenses offset, in part, by an increase in the provision for income taxes, all discussed above. The increase in net income in the nine months ended resulted from the increase in gross profit offset, in part, by an increase in selling, general and administrative expenses and an increase in the provision for income taxes, all discussed above.

Liquidity and Capital Resources

The Company's working capital is an appropriate indicator of the liquidity of its business, and during the past two fiscal years, the Company, when possible, has funded all of its operations with cash flows resulting from operating activities and when necessary from its existing cash and investments. The Company did not borrow any funds during the last two fiscal years. Management has available a \$3,000,000 line of credit to help fund further growth or working capital needs, if necessary, but does not anticipate the need for any borrowed funds in the foreseeable future. Contingent liabilities on outstanding standby letters of credit agreements aggregated to zero at March 31, 2022 and 2021. The existing line of credit was extended and expires February 28, 2023.

The Company's working capital as of March 31, 2022 and 2021 was approximately \$28.7 million and \$26.1 million, respectively. The Company may at times be required to repurchase shares at the ESOP participants' request at the fair market value. During the three and nine months ended March 31, 2022 and 2021, the Company did not repurchase any shares held by the ESOP. Under existing authorizations from the Company's Board of Directors, as of March 31, 2022, management is authorized to purchase an additional \$783,460 of Company stock.

[Index](#)

The table below presents the summary of cash flow information for the fiscal years indicated:

	Nine Months Ended March 31,	
	2022	2021
Net cash provided by operating activities	\$ 811,078	\$ 2,188,300
Net cash (used in) provided by investing activities	(330,958)	2,099,830
Net cash used in financing activities	—	(1,201,316)

Net cash provided by operating activities fluctuates between periods primarily as a result of differences in sales and net income, provision for income taxes, the timing of the collection of accounts receivable, purchase of inventory, and payment of accounts payable. The decrease in cash provided by operating activities compared to the prior year primarily relates to the decrease in cash collected from trade receivables offset, in part, by an increase in net income and the decrease in inventory purchases. Net cash used in investing activities increased in the nine months ended March 31, 2022 as compared to the same period in 2021 primarily due to the reinvestment of matured securities when compared to the same period last year. During the nine months ended March 31, 2022, there was no cash used for financing activities primarily resulting from the suspension of the regular dividend. In the prior year, cash used in financing activities resulted from the payment of regular dividends.

The Company currently believes that the cash flow generated from operations and when necessary, from cash and cash equivalents will be sufficient to meet its long-term funding requirements for the foreseeable future.

During the nine months ended March 31, 2022 and 2021, the Company expended \$216,500 and \$34,337, respectively, for plant improvements and new equipment. The Company originally budgeted approximately \$200,000 for new equipment and plant improvements in fiscal year 2022. Expenditures for new equipment and plant improvements are now expected to approximate \$400,000 for the current fiscal year, attributable to the need to accelerate a building roof restoration project, originally expected to occur in a future fiscal year. Management anticipates that the funds required will be available from current operations.

CAUTIONARY STATEMENT FOR PURPOSES OF THE "SAFE HARBOR" PROVISIONS OF THE PRIVATE
SECURITIES LITIGATION REFORM ACT OF 1995

This report contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. The terms "believe," "anticipate," "intend," "goal," "expect," and similar expressions may identify forward-looking statements. These forward-looking statements represent the Company's current expectations or beliefs concerning future events. The matters covered by these statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those set forth in the forward-looking statements, including the Company's dependence on timely development, introduction and customer acceptance of new products, the impact of competition and price erosion, supply and manufacturing constraints, potential new orders from customers, the impact of cyber or other security threats or other disruptions to our business, the impact of the COVID-19 pandemic on the United States economy and our operations and other risks and uncertainties. The foregoing list should not be construed as exhaustive, and the Company disclaims any obligation subsequently to revise any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company is a smaller reporting company as defined under Securities and Exchange Commission Rule 12b-2. Pursuant to the exemption available to smaller reporting company issuers under Item 305 of Regulation S-K, quantitative and qualitative disclosures about market risk, the Company is not required to provide the information for this item.

Item 4. Controls and Procedures

(a) The Company's management, with the participation of the Company's chief executive officer and chief financial officer, carried out an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

(b) There have been no changes in our internal controls over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

[Index](#)

PART II: Other Information and Signatures

- Item 1. Legal Proceedings
None
- Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
- (a) Securities Sold
None
- (c) Securities Repurchased
As of March 31, 2022 the Company can repurchase up to \$783,460 of its common stock pursuant to an ongoing plan authorized by the Board of Directors. During the quarter ended March 31, 2022 no shares were repurchased.
- Item 3. Defaults Upon Senior Securities
None
- Item 4. Mine Safety Disclosures
Not applicable
- Item 5. Other Information
None
- Item 6. Exhibits
- 31.1 [Certification of the Chief Executive Officer pursuant to Rules 13a-14\(a\) and 15d-14\(a\) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002](#)
- 31.2 [Certification of the Principal Financial Officer pursuant to Rules 13a-14\(a\) and 15d-14\(a\) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002](#)
- 32.1 [Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002](#)
- 32.2 [Certification of the Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002](#)

[Index](#)

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.

ESPEY MFG. & ELECTRONICS CORP.

/s/ David O'Neil

David O'Neil
President and Chief Executive Officer

/s/Katrina Sparano

Katrina Sparano
Principal Financial Officer

Date: May 16, 2022

EXHIBIT 31.1

Certification of the Chief Executive Officer

Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934,
as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, David O'Neil, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Espey Mfg. & Electronics Corp;
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 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report 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
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. 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 registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 16, 2022

/s/ David O'Neil

David O'Neil

President and Chief Executive Officer

EXHIBIT 31.2
Certification of the Principal Financial Officer
Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934,
as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Katrina Sparano, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Espey Mfg. & Electronics Corp;
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 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report 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
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. 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 registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 16, 2022

/s/ Katrina Sparano

Katrina Sparano
Principal Financial Officer

EXHIBIT 32.1

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

In connection with this quarterly report of Espey Mfg. & Electronics Corp. (the "Company") on Form 10-Q for the period ended March 31, 2022 as filed with the Securities and Exchange Commission on the date hereof (the "report"), I, David O'Neil, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 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 this report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 16, 2022

/s/ David O'Neil

David O'Neil

President and Chief Executive Officer

EXHIBIT 32.2

Certification of the Principal Financial Officer pursuant to 18 U.S.C. Section 1350,
as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with this quarterly report of Espey Mfg. & Electronics Corp. (the "Company") on Form 10-Q for the period ended March 31, 2022 as filed with the Securities and Exchange Commission on the date hereof (the "report"), I, Katrina Sparano, Principal Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 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 this report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 16, 2022

/s/Katrina Sparano

Katrina Sparano
Principal Financial Officer