

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 **October 31, 2016**

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

For the transition period from _____ to _____

Commission File Number **0-1678**

BUTLER NATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

Kansas

41-0834293

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

19920 West 161st Street, Olathe, Kansas 66062

(Address of principal executive offices)(Zip Code)

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days: Yes 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. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.:

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

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

The number of shares outstanding of the Registrant's Common Stock, \$0.01 par value, as of December 9, 2016 was 64,066,873 shares.

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
As of October 31, 2016 and April 30, 2016
(in thousands except per share data)

	October 31, 2016 (unaudited)	April 30, 2016
ASSETS		
CURRENT ASSETS:		
Cash	\$ 6,446	\$ 7,381
Accounts receivable	3,228	1,574
Inventories		
Raw materials	6,145	6,339
Work in process	1,215	1,349
Finished goods	247	275
Total inventory	<u>7,607</u>	<u>7,963</u>
Prepaid expenses and other current assets	<u>989</u>	<u>873</u>
Total current assets	<u>18,270</u>	<u>17,791</u>
PROPERTY, PLANT AND EQUIPMENT:		
Land and building	4,099	4,081
Aircraft	5,888	5,712
Machinery and equipment	3,694	3,630
Office furniture and fixtures	6,022	5,637
Leasehold improvements	<u>4,032</u>	<u>4,032</u>
	23,735	23,092
Accumulated depreciation	<u>(13,973)</u>	<u>(13,218)</u>
Total property, plant and equipment	<u>9,762</u>	<u>9,874</u>
SUPPLEMENTAL TYPE CERTIFICATES (net of accumulated amortization of \$3,945 at October 31, 2016 and \$3,549 at April 30, 2016)		
	<u>6,353</u>	<u>6,481</u>
OTHER ASSETS:		
Deferred tax asset	686	1,104
Other assets (net of accumulated amortization of \$6,225 at October 31, 2016 and \$5,579 at April 30, 2016)	<u>6,801</u>	<u>7,447</u>
Total other assets	<u>7,487</u>	<u>8,551</u>
Total assets	<u>\$ 41,872</u>	<u>\$ 42,697</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Promissory notes	\$ 2,758	\$ 3,988
Current maturities of long-term debt	2,110	2,464
Accounts payable	1,640	2,018
Customer deposits	1,730	258
Gaming facility mandated payment	1,095	1,206
Compensation and compensated absences	1,132	1,322
Other current liabilities	<u>242</u>	<u>125</u>
Total current liabilities	10,707	11,381
LONG-TERM DEBT, NET OF CURRENT MATURITIES		
	<u>4,212</u>	<u>5,218</u>
Total liabilities	<u>14,919</u>	<u>16,599</u>
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock, par value \$5:		
Authorized 50,000,000 shares, all classes		
Designated Classes A and B 200,000 shares		
\$100 Class A, 9.8 %, cumulative if earned liquidation and redemption value \$100, no shares issued and outstanding	-	-
\$1,000 Class B, 6 %, convertible cumulative, liquidation and redemption value \$1,000, no shares issued and outstanding	-	-
Common stock, par value \$.01: authorized 100,000,000 shares issued and outstanding 64,066,873 shares at October 31, 2016 and 64,066,873 shares at April 30, 2016	640	640
Capital contributed in excess of par	13,356	13,716
Treasury stock at cost, 600,000 shares	(732)	(732)
Retained earnings	<u>9,288</u>	<u>8,185</u>
Total stockholders' equity Butler National Corporation	22,552	21,809
Noncontrolling interest in BHCMC, LLC	<u>4,401</u>	<u>4,289</u>
Total stockholders' equity	<u>26,953</u>	<u>26,098</u>
Total liabilities and stockholders' equity	<u>\$ 41,872</u>	<u>\$ 42,697</u>

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED OCTOBER 31, 2016 AND 2015
(in thousands, except per share data)
(unaudited)

	THREE MONTHS ENDED	
	October 31,	
	2016	2015
REVENUE:		
Professional Services	\$ 7,722	\$ 7,334
Aerospace Products	5,091	2,772
Total revenue	<u>12,813</u>	<u>10,106</u>
COSTS AND EXPENSES:		
Cost of Professional Services	4,649	4,539
Cost of Aerospace Products	3,698	2,449
Marketing and advertising	1,064	1,137
Employee benefits	438	429
Depreciation and amortization	507	566
General, administrative and other	1,293	1,585
Total costs and expenses	<u>11,649</u>	<u>10,705</u>
OPERATING INCOME (LOSS)	<u>1,164</u>	<u>(599)</u>
OTHER INCOME (EXPENSE):		
Interest expense	(106)	(117)
Other income (expense), net	1	9
Total other expense	<u>(105)</u>	<u>(108)</u>
INCOME (LOSS) BEFORE INCOME TAXES	1,059	(707)
PROVISION (BENEFIT) FOR INCOME TAXES		
Deferred income tax expense	292	-
Provision (benefit) for income taxes	<u>-</u>	<u>(269)</u>
NET INCOME (LOSS)	767	(438)
Net income attributable to noncontrolling interest in BHCMC, LLC	(248)	(40)
NET INCOME (LOSS) ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION	<u>\$ 519</u>	<u>\$ (478)</u>
BASIC EARNINGS (LOSS) PER COMMON SHARE	<u>\$ 0.01</u>	<u>\$ (0.01)</u>
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	<u>63,466,873</u>	<u>62,260,098</u>
DILUTED EARNINGS (LOSS) PER COMMON SHARE	<u>\$ 0.01</u>	<u>\$ (0.01)</u>
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	<u>63,466,873</u>	<u>62,260,098</u>

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE SIX MONTHS ENDED OCTOBER 31, 2016 AND 2015
(in thousands, except per share data)
(unaudited)

	SIX MONTHS ENDED	
	October 31,	
	2016	2015
REVENUE:		
Professional Services	\$ 15,206	\$ 14,938
Aerospace Products	8,996	6,864
Total revenue	<u>24,202</u>	<u>21,802</u>
COSTS AND EXPENSES:		
Cost of Professional Services	9,169	9,042
Cost of Aerospace Products	6,569	5,570
Marketing and advertising	2,083	2,581
Employee benefits	914	914
Depreciation and amortization	1,014	1,177
General, administrative and other	2,578	2,757
Total costs and expenses	<u>22,327</u>	<u>22,041</u>
OPERATING INCOME (LOSS)	<u>1,875</u>	<u>(239)</u>
OTHER INCOME (EXPENSE):		
Interest expense	(224)	(236)
Other income (expense), net	(18)	10
Total other expense	<u>(242)</u>	<u>(226)</u>
INCOME (LOSS) BEFORE INCOME TAXES	1,633	(465)
PROVISION (BENEFIT) FOR INCOME TAXES		
Deferred income tax expense	418	-
Provision (benefit) for income taxes	<u>-</u>	<u>(258)</u>
NET INCOME (LOSS)	1,215	(207)
Net income attributable to noncontrolling interest in BHCMC, LLC	(472)	(252)
NET INCOME (LOSS) ATTRIBUTABLE TO BUTLER NATIONAL CORPORATION	<u>\$ 743</u>	<u>\$ (459)</u>
BASIC EARNINGS (LOSS) PER COMMON SHARE	<u>\$ 0.01</u>	<u>\$ (0.01)</u>
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	<u>63,466,873</u>	<u>62,260,098</u>
DILUTED EARNINGS (LOSS) PER COMMON SHARE	<u>\$ 0.01</u>	<u>\$ (0.01)</u>
WEIGHTED AVERAGE SHARES USED IN PER SHARE CALCULATION	<u>63,466,873</u>	<u>62,260,098</u>

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED OCTOBER 31, 2016 AND 2015
(in thousands)
(unaudited)

	SIX MONTHS ENDED October 31,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	\$ 1,215	\$ (207)
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Depreciation and amortization	1,797	2,027
Changes in assets and liabilities		
Accounts receivable	(1,654)	(261)
Inventories	356	(948)
Prepaid expenses and other current assets	(116)	(31)
Deferred tax asset	418	(258)
Accounts payable	(378)	(189)
Customer deposits	1,472	282
Accrued liabilities	(190)	(295)
Gaming facility mandated payment	(111)	88
Other current liabilities	117	149
Net cash provided by operating activities	2,926	357
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(911)	(602)
Net cash used in investing activities	(911)	(602)
CASH FLOWS FROM FINANCING ACTIVITIES		
Borrowings of promissory notes, net	(1,230)	1,218
Borrowings of long-term debt	-	70
Repayments of long-term debt	(1,360)	(1,256)
Distribution to non-controlling member	(360)	(360)
Net cash used in financing activities	(2,950)	(328)
NET DECREASE IN CASH	(935)	(573)
CASH, beginning of period	7,381	6,195
CASH, end of period	\$ 6,446	\$ 5,622
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid	\$ 225	\$ 237
Income taxes paid	\$ -	\$ -

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except per share data)
(unaudited)

1. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Therefore, these financial statements should be read in conjunction with the annual report on Form 10-K for the fiscal year ended April 30, 2016. In our opinion, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three and six months ended October 31, 2016 are not indicative of the results of operations that may be expected for the fiscal year ended April 30, 2017.

Certain reclassifications within the condensed financial statement captions have been made to maintain consistency in presentation between years. These reclassifications have no impact on the reported results of operations. Financial amounts are in thousands of dollars except per share amounts.

2. Net Income (Loss) Per Share: Butler National Corporation ("the Company") follows ASC 260 that requires the reporting of both basic and diluted earnings per share. Basic earnings per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. In accordance with ASC 260, any anti-dilutive effects on net earnings (loss) per share are excluded. The number of potential common shares as of October 31, 2016 is 63,466,873.

3. Research and Development: We invested in research and development activities. The amount invested in the six months ended October 31, 2016 and 2015 was \$717 and \$937 respectively.

4. Debt: At October 31, 2016, the Company was utilizing a line of credit totaling \$5,000. The unused line at October 31, 2016 was \$2,242. These funds were primarily used for the purchase of inventories and aircraft modification Supplemental Type Certificate ("STC") development costs for modifications and avionics. The line of credit is due on demand and is collateralized by the first and second positions on all assets of the Company.

At October 31, 2016, there are three notes collateralized by aircraft security agreements totaling \$586. These notes were used for the purchase and modifications of these collateralized aircraft and Butler Avionics, Inc.

There are three notes at a bank totaling \$713 for real estate located in Olathe, Kansas and Tempe, Arizona. The due date for the notes is March 2019.

One note totaling \$283 remains for real estate purchased in Dodge City, Kansas and matures in June 2019.

BHCMC arranged to acquire for ownership by the Kansas Lottery additional gaming machines. The balance of these financed payables is \$652.

One note secured by all of the BNSC assets and compensation due under the State Management contract totals \$4,088 and matures in May 2020. The proceeds were used primarily to retire obligations with BHCI (a non-controlling owner of BHCMC, LLC).

We are not in default of any of our notes as of October 31, 2016.

We believe that our current banks will provide the necessary capital for our business operations. However, we continue to maintain contact with other banks that have an interest in funding our working capital needs to continue our growth in operations in 2017 and beyond.

5. Other Assets: Our other asset account includes assets of \$5,500 related to the Kansas Expanded Lottery Act Management Contract privilege fee, \$4,576 of gaming equipment we were required to pay for ownership by the State of Kansas Lottery, and JET autopilot intellectual property of \$1,417 and miscellaneous other assets of \$1,533. BHCMC expects the \$5,500 privilege fee to have a value

over the remaining life of the Management Contract with the State of Kansas which will end in December 2024. There is no assurance of the Management Contract renewal. The Managers Certificate asset for use of gaming equipment is being amortized over a period of three years based on the estimated useful life of gaming equipment. The JET intellectual property is being amortized over a period of 15 years.

6. Stock Options: At October 31, 2016 we had no outstanding stock options. There were 7,262,064 outstanding stock options that were issued on December 31, 2010 all of which expired on December 31, 2015.

7. Subsequent Events: The Company evaluated its October 31, 2016 financial statements for subsequent events through the filing date of this report. The Company is not aware of any subsequent events that would require recognition or disclosure in the financial statements.

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

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

Forward-Looking Statements

Statements made in this report, filed with the Securities and Exchange Commission, communications to stockholders, press releases, and oral statements made by representatives of the Company that are not historical in nature, or that state the Company or management intentions, hopes, beliefs, expectations or predictions of the future, may constitute "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements can often be identified by the use of forward-looking terminology, such as "could," "should," "will," "intended," "continue," "believe," "may," "expect," "hope," "anticipate," "goal," "forecast," "plan," "guidance" or "estimate" or the negative of these words, variations thereof or similar expressions. Forward-looking statements are not guarantees of future performance or results. They involve risks, uncertainties, and assumptions. It is important to note that any such performance and actual results, financial condition or business, could differ materially from those expressed in such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those set forth in Item 1A. (Risk Factors) of this Quarterly Report on Form 10-Q, and Item 1A. (Risk Factors) to the Company's Annual Report on Form 10-K for the fiscal year ended April 30, 2016 and reference to the Cautionary Statements filed by us as Exhibit 99 to the most recent Annual Report on Form 10-K. Other unforeseen factors not identified herein could also have such an effect. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes in future operating results, financial condition or business over time.

The forward-looking statements in this report are only predictions and actual events or results may differ materially. In evaluating such statements, a number of risks, uncertainties and other factors could cause actual results, performance, financial condition, cash flows, prospects and opportunities to differ materially from those expressed in, or implied by, the forward-looking statements. These risks, uncertainties and other factors include those set forth in Item 1A (Risk Factors) of the Company's Annual Report on Form 10-K and the Cautionary Statements filed by us as Exhibit 99 to this form, including the following factors:

- the impact of general economic trends on the Company's business;
- sensitivity of demand related to changes in the U.S. dollar to foreign currency exchange rates;
- the deferral or termination of programs or contracts for convenience by customers;
- market acceptance of the Company's Aerospace Products and or other planned products or product enhancements;
- increased fuel and energy costs and the downward pressure on demand for our aircraft business;
- the ability to gain and maintain regulatory approval of existing products and services and receive regulatory approval of new businesses and products;
- the actions of regulatory, legislative, executive or judicial decisions of the federal, state or local level with regard to our business and the impact of any such actions;
- failure to retain/recruit key personnel;
- the availability of government funding to vendors and customers;
- any delays in receiving components from third party suppliers;
- the competitive environment;

- the bankruptcy or insolvency of one or more key customers or vendors;
- new product offerings from competitors;
- protection of intellectual property rights;
- the ability to service, supply or visit the international market;
- acts of terrorism and war and other uncontrollable events;
- joint ventures and other arrangements;
- low priced penny-stock regulations;
- general governance features;
- United States and other country defense spending cuts;
- our estimated effective income tax rates; estimated tax benefits; and merits of our tax position;
- potential future acquisitions;
- changes in laws, including increased tax rates, smoking bans, regulations or accounting standards, third-party relations and approvals, and decisions, disciplines and fines of courts, regulators and governmental bodies;
- the ability to timely and cost-effectively integrate companies that we acquire into our operations;
- construction factors, including delays, increased costs of labor and materials, availability of labor and materials, zoning issues, environmental restrictions, soil and water conditions, weather and other hazards, site access matters and building permit issues;
- litigation outcomes and judicial and governmental body actions, including gaming legislative action, referenda, regulatory disciplinary actions and fines and taxation;
- access to insurance on reasonable terms for our assets;
- cybersecurity incidents could disrupt business operations, result in the loss of critical and confidential information, and adversely impact our reputation and results of operations;
- as a supplier of military and other equipment to the U.S. Government, we are subject to unusual risks, such as the right of the U.S. Government contractor to terminate contracts for convenience and to conduct audits and investigations of our operations and performance;
- our reputation and ability to do business may be impacted by the improper conduct of employees, vendors, agents or business partners;
- changes in legislation or government regulations or policies can have a significant impact on our results of operations; and
- other factors disclosed from time to time in the Company's filings with the Securities and Exchange Commission.

Except as expressly required by the federal securities laws, the Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise after the date of this report. Results of operations in any past period should not be considered indicative of the results to be expected for future periods. Fluctuations in operating results may also result in fluctuations in the price of the Company's common stock.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Form 10-Q. The Company does not undertake any obligation to publicly release any revisions to these forward-looking statements to reflect events, circumstances or changes in expectations after the date of this Form 10-Q, or to reflect the occurrence of unanticipated events. The forward-looking statements in this document are intended to be subject to the safe harbor protection provided by Sections 27A of the Securities Act of 1933, as amended (the "Securities Act") and 21E of the Securities Exchange Act of 1934 as amended.

Investors should also be aware that while the Company, from time to time, communicates with securities analysts; it is against its policy to disclose any material non-public information or other confidential commercial information. Accordingly, shareholders should not assume that the Company agrees with any statement or report issued by any analyst irrespective of the content of the statement or report. Furthermore, the Company has a policy against issuing or confirming financial forecasts or projections issued by others. Thus, to the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are **not** the responsibility of Butler National Corporation.

Management Overview

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

Our revenue is primarily derived from two very different business segments; Aerospace Products and Professional Services. These segments operate through various Butler National subsidiaries and affiliates listed in the Company's fiscal year 2016 annual report on Form 10-K.

Aerospace Products

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

Aerospace is the legacy part of the Butler National business. Organized over 56 years ago, this business is based upon design engineering and installation innovations to enhance and support products related to airplanes and ground support equipment. These new products included: in the 1960's, aircraft electronic load sharing and system switching equipment, a number of airplane electronic navigation instruments, radios and transponders; in the 1970's, ground based VOR navigation equipment sold worldwide and GPS equipment as we know it today in civilian use; in the 1980's, special mission modifications to business jets for aerial surveillance and conversion of passenger configurations to cargo; in the 1990's, classic aviation support of aging airplanes with enhanced protection of electrical systems through transient suppression devices (TSD), control electronics for military weapon systems and improved aerodynamic control products (Avcon Fins) allowing stability at higher gross weights for additional special mission applications; in the 2000's, improved accuracy of the airspeed and altimeter systems to allow less vertical separation between flying airplanes (RVSM) and acquisition of the JET autopilot product line to support and replace aged electronic equipment in the classic fleet of Learjet airplanes; and in the 2010's, the acquisition of Butler Avionics to provide additional classic airplane support by retrofit of avionics from the past 40 years to modern state of the art equipment for sale worldwide using FAA supplemental type certification (STC). Aerospace is preparing for the 2020's through the development and certification of ADS-B systems in support of the FAA "NextGen" update of the Air Traffic Control system in the United States and many other countries.

Aerospace continues to be a focus for new product design and development. Butler National received FAA approvals of a number of products: Butler National's newly redesigned rate gyroscope for Learjets; the replacement vertical accelerometer safety device that resolves obsolescence as a key component of the legacy Learjet stall warning systems; Butler National's addition of the GARMIN GTN 650/750 Global Position System Navigator with Communication transceiver in the Learjet Model 30 series and 20 series, Avcon's new cargo/sensor carrying pod that mounts to the bottom of a King Air Model 90 airplane, and the provisions for external stores on a Learjet Model 60 to enable the 60 for consideration as the next Learjet candidate for special mission operations; and noise suppression for Learjet 20 series aircraft. We expect this segment will continue to grow in the future. To address the three to five year business cycles related to the Aerospace industry, in the 1990's, we began providing Professional Services to markets outside the Aerospace industry.

Professional Services

Professional Services derives its revenue from (a) professional management services in the gaming industry through Butler National Service Corporation ("BNSC") and BHCMC, LLC ("BHCMC"), and (b) professional architectural, engineering and management support services.

In the early 1990's, management determined that more revenue stable business units were needed to sustain the Company. Members of the Board of Directors had contacts with several American Indian tribes and other members of the Board were associated with gaming operators in Las Vegas. After enactment of the 1988 Indian Gaming Regulatory Act ("IGRA") we reached out to various Indian tribes with land in the area to explore the opportunities for operations under IGRA. This resulted in the "Stables", an Indian owned casino on Modoc Indian land opened in September 1998 developed and managed by BNSC. The Stables Management Agreement has been available on the website maintained by the National Indian Gaming Commission ("NIGC"). The Stables Management Agreement was subsequently amended by various amendments dated April 30, 2003 (the "First Amendment"), November 30, 2006 (the "Second Amendment"), October 19, 2009 (the "Third Amendment") and September 22, 2011 (the "Fourth Amendment"). The result of the First Amendment, Second Amendment, Third Amendment and Fourth Amendment is to provide (a) that twenty (20%) of net profits from the Stables are distributed to BNSC, (b) to end per the joint venture agreement the participation of the Miami Indian tribe from the business and (c) to extend the duration of the Stables Management Agreement through September 30, 2018.

From this experience with IGRA and the success of the Indian gaming industry, we determined that the IGRA model may be

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

The terms of the agreement between the Kansas Lottery and BNSC/BHCMC required the completion of an addition to the Boot Hill Casino. The Phase II expansion of Boot Hill Casino began in early 2012 and was completed in January 2013. Phase II expansion of the unfinished gaming floor space built during Phase I construction and tenant improvements was funded by tenant improvement leases, gaming machine acquisitions, and casino earnings. The Phase II expansion included the interior finish of 15,000 square feet of casino shell and provided for up to 216 additional gaming machines. Part of the expansion included a breezeway connecting the Boot Hill Casino and the Dodge City special events center (United Wireless Arena). Boot Hill Casino now has approximately 650 gaming machines on the floor. Boot Hill Casino acquired the naming rights to the City of Dodge City and Ford County owned conference center connected to the casino through the breezeway. The conference center is now known as the Boot Hill Casino and Resort Conference Center.

Results Overview

The six months ending October 31, 2016 revenue increased 11% to \$24.2 million compared to \$21.8 million in the six months ending October 31, 2015. In the six months ending October 31, 2016 the professional services revenue was \$15.2 million compared to \$14.9 million in the six months ending October 31, 2015, an increase of 2%. In the six months ending October 31, 2016 the Aerospace Products revenue was \$9.0 million compared to \$6.9 million in the six months ending October 31, 2015, an increase of 31%.

The six months ending October 31, 2016 net income increased to \$743 compared to a net loss of \$459 in the six months ending October 31, 2015. The six months ending October 31, 2016, operating income increased to \$1.9 million, from an operating loss of \$239 in the six months ending October 31, 2015.

RESULTS OF OPERATIONS

SIX MONTHS ENDING OCTOBER 31, 2016 COMPARED TO SIX MONTHS ENDING OCTOBER 31, 2015

(dollars in thousands)	Six Months Ended October 31, 2016	Percent of Total Revenue	Six Months Ended October 31, 2015	Percent of Total Revenue	Percent Change 2015-2016
Revenue:					
Professional Services	\$ 15,206	63%	\$ 14,938	69%	2%
Aerospace Products	8,996	37%	6,864	31%	31%
Total revenue	<u>24,202</u>	100%	<u>21,802</u>	100%	11%
Costs and expenses:					
Costs of Professional Services	9,169	38%	9,042	41%	1%
Cost of Aerospace Products	6,569	27%	5,570	26%	18%
Marketing and advertising	2,083	8%	2,581	12%	(19)%
Employee benefits	914	4%	914	4%	0%
Depreciation and amortization	1,014	4%	1,177	5%	(14)%
General, administrative and other	2,578	11%	2,757	13%	(6)%
Total costs and expenses	<u>22,327</u>	92%	<u>22,041</u>	101%	1%
Operating income (loss)	<u>\$ 1,875</u>	8%	<u>\$ (239)</u>	(1)%	

Revenue:

Revenue increased 11% to \$24.2 million in the six months ended October 31, 2016, compared to \$21.8 million in the six months ended October 31, 2015. See "Operations by Segment" below for a discussion of the primary reasons for the increase in revenue.

- Professional Services derives its revenue from (a) professional management services in the gaming industry through Butler National Service Corporation ("BNSC") and BHCMC, LLC ("BHCMC"), and (b) professional architectural, engineering and management support services. Revenue from Professional Services increased 2% for the six months to \$15.2 million at October 31, 2016 compared to \$14.9 million at October 31, 2015.
- Aerospace Products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft. Aerospace Products revenue increased 31% for the six months to \$9.0 million at October 31, 2016 compared to \$6.9 million at October 31, 2015. This increase is primarily due to an increase in avionics-related revenue of \$1.9 million. We anticipate future domestic military spending reductions and continued slow growth of the United States economy.

Costs and expenses:

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

Costs and expenses increased 1% in the six months ended October 31, 2016 to \$22.3 million compared to \$22.0 million in the six months ended October 31, 2015. Costs and expenses were 92% of total revenue in the six months ended October 31, 2016, as compared to 101% of total revenue in the six months ended October 31, 2015.

Costs of Professional Services remained constant in the six months ended October 31, 2016 at \$9.2 million compared to \$9.0 million in the six months ended October 31, 2015. Costs were 38% of total revenue in the six months ended October 31, 2016, as compared to 41% of total revenue in the six months ended October 31, 2015.

Costs of Aerospace Products increased by 18% in the six months ended October 31, 2016 to \$6.6 million compared to \$5.6 million for the six months ended October 31, 2015. Costs were 27% of total revenue in the six months ended October 31, 2016, as compared to 26% of total revenue in the six months ended October 31, 2015.

Marketing and advertising expenses decreased by 19% in the six months ended October 31, 2016, to \$2.1 million compared to \$2.6 million in the six months ended October 31, 2015. Expenses were 8% of total revenue in the six months ended October 31, 2016, as compared to 12% of total revenue in the six months ended October 31, 2015. Marketing and advertising expenses include advertising, sales and marketing labor, gaming development costs, and casino and product promotions.

Employee benefits expenses as a percent of total revenue was 4% in the six months ended October 31, 2016, compared to 4% in the six months ended October 31, 2015. These expenses remained constant at \$914 in the six months ended October 31, 2016, and \$914 in the six months ended October 31, 2015. These expenses include the employers' share of all federal, state and local taxes, paid time off for vacation, holidays and illness, employee health and life insurance programs and employer matching contributions to retirement plans.

Depreciation and amortization expenses as a percent of total revenue was 4% in the six months ended October 31, 2016, compared to 5% in the six months ended October 31, 2015. These expenses decreased 14% to \$1.0 million in the six months ended October 31, 2016, from \$1.2 million in the six months ended October 31, 2015. These expenses include depreciation related to owned assets being depreciated over various useful lives and amortization of intangible items including the Kansas privilege fee related to the Boot Hill Casino being expensed over the term of the gaming contract with the State of Kansas. Phase II expansion to Boot Hill Casino was formally completed in early January 2013 and we began depreciation on \$4.9 million of assets with various useful lives. BHCMC, LLC depreciation and amortization expense for the six months ended October 31, 2016 was \$703 compared to \$671 in the six months ended October 31, 2015.

General, administrative and other expenses as a percent of total revenue was 11% in the six months ended October 31, 2016, compared to 13% in the six months ended October 31, 2015. These expenses decreased 6% to \$2.6 million in the six months ended October 31, 2016, from \$2.8 million in the six months ended October 31, 2015.

Other income (expense):

Other income (expense) was (\$242) in the six months ended October 31, 2016, compared with other income (expense) of (\$226) in the six months ended October 31, 2015. Interest related to obligations of BHCMC, LLC was \$109 in the six months ended October 31, 2016 compared to \$124 in the six months ended October 31, 2015.

Operations by Segment

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

The following table presents a summary of our operating segment information for the six months ended October 31, 2016 and October 31, 2015:

(dollars in thousands)	Six Months Ended <u>October 31, 2016</u>	Percent of Total Revenue	Six Months Ended <u>October 31, 2015</u>	Percent of Total Revenue	Percent Change <u>2015-2016</u>
Professional Services					
Revenue					
Boot Hill Casino	\$ 14,956	98%	\$ 14,517	97%	3%
Management/Professional Services	<u>250</u>	<u>2%</u>	<u>421</u>	<u>3%</u>	<u>(41)%</u>
Revenue	15,206	100%	14,938	100%	2%
Costs of Professional Services	9,169	60%	9,042	61%	1%
Expenses	<u>5,086</u>	<u>34%</u>	<u>5,435</u>	<u>36%</u>	<u>(6)%</u>
Total costs and expenses	<u>14,255</u>	<u>94%</u>	<u>14,477</u>	<u>97%</u>	<u>(2)%</u>
Professional Services operating income before noncontrolling interest in BHCMC, LLC	<u>\$ 951</u>	<u>6%</u>	<u>\$ 461</u>	<u>3%</u>	<u>106%</u>

(dollars in thousands)	Six Months Ended <u>October 31, 2016</u>	Percent of Total Revenue	Six Months Ended <u>October 31, 2015</u>	Percent of Total Revenue	Percent Change <u>2015-2016</u>
Aerospace Products					
Revenue	\$ 8,996	100%	\$ 6,864	100%	31%
Costs of Aerospace Products	6,569	73%	5,570	81%	18%
Expenses	<u>1,503</u>	<u>17%</u>	<u>1,994</u>	<u>29%</u>	<u>(25)%</u>
Total costs and expenses	<u>8,072</u>	<u>90%</u>	<u>7,564</u>	<u>110%</u>	<u>7%</u>
Aerospace Products operating income (loss)	<u>\$ 924</u>	<u>10%</u>	<u>\$ (700)</u>	<u>(10)%</u>	

Professional Services

- Revenue from Professional Services increased 2% for the six months ended October 31, 2016 to \$15.2 million compared to \$14.9 million for the six months ended October 31, 2015.

In the six months ended October 31, 2016 Boot Hill Casino received gross receipts for the State of Kansas of \$19.9 million compared to \$19.7 million for the six months ended October 31, 2015. Mandated fees, taxes and distributions reduced gross receipts by \$6.6 million resulting in gaming revenue of \$13.3 million for the six months ended October 31, 2016, compared to a reduction to gross receipts of \$6.7 million resulting in gaming revenue of \$13.0 million for the six months ended October 31, 2015. Non-gaming revenue at Boot Hill Casino remained constant at \$1.6 million for the six months ended October 31, 2016, and \$1.6 million for the six months ended October 31, 2015.

The remaining management and Professional Services revenue includes professional management services in the gaming industry, and licensed architectural services. Professional Services revenue excluding Boot Hill Casino decreased 41% to \$250 for the six months ended October 31, 2016, compared to \$421 for the six months ended October 31, 2015.

- Costs of Professional Services increased 1% in the six months ended October 31, 2016 to \$9.2 million compared to \$9.0 million in the six months ended October 31, 2015. Costs were 60% of segment total revenue in the six months ended October 31, 2016, as compared to 61% of segment total revenue in the six months ended October 31, 2015.
- Expenses decreased 6% in the six months ended October 31, 2016 to \$5.1 million compared to \$5.4 million in the six months ended October 31, 2015. Expenses were 34% of segment total revenue in the six months ended October 31, 2016, as compared to 36% of segment total revenue in the six months ended October 31, 2015.

Aerospace Products

- Revenue increased 31% to \$9.0 million in the six months ended October 31, 2016, compared to \$6.9 million in the six months ended October 31, 2015. We anticipate future domestic military spending reductions and continued slow growth of the United States economy. In an effort to offset decreased domestic military spending, we have invested in the development of several STCs. These STCs are state of the art avionics and we are aggressively marketing both domestically and internationally.
- Costs of Aerospace Products increased by 18% in the six months ended October 31, 2016 to \$6.6 million compared to \$5.6 million for the six months ended October 31, 2015. Costs were 73% of segment total revenue in the six months ended October 31, 2016, as compared to 81% of segment total revenue in the six months ended October 31, 2015.
- Expenses decreased 25% in the six months ended October 31, 2016 to \$1.5 million compared to \$2.0 million in the six months ended October 31, 2015. Expenses were 17% of segment total revenue in the six months ended October 31, 2016, as compared to 29% of segment total revenue in the six months ended October 31, 2015.

SECOND QUARTER FISCAL 2017 COMPARED TO SECOND QUARTER FISCAL 2016

(dollars in thousands)	Three Months Ended October 31, 2016	Percent of Total Revenue	Three Months Ended October 31, 2015	Percent of Total Revenue	Percent Change 2015-2016
Revenue:					
Professional Services	\$ 7,722	60%	\$ 7,334	73%	5%
Aerospace Products	5,091	40%	2,772	27%	84%
Total revenue	<u>12,813</u>	<u>100%</u>	<u>10,106</u>	<u>100%</u>	<u>27%</u>
Costs and expenses:					
Costs of Professional Services	4,649	36%	4,539	45%	2%
Cost of Aerospace Products	3,698	29%	2,449	24%	51%
Marketing and advertising	1,064	8%	1,137	11%	(6)%
Employee benefits	438	4%	429	4%	2%
Depreciation and amortization	507	4%	566	6%	(10)%
General, administrative and other	1,293	10%	1,585	16%	(18)%
Total costs and expenses	<u>11,649</u>	<u>91%</u>	<u>10,705</u>	<u>106%</u>	<u>9%</u>
Operating income (loss)	<u>\$ 1,164</u>	<u>9%</u>	<u>\$ (599)</u>	<u>(6)%</u>	

Revenue:

Revenue increased 27% to \$12.8 million in the three months ended October 31, 2016, compared to \$10.1 million in the three months ended October 31, 2015. See "Operations by Segment" below for a discussion of the primary reasons for the increase in revenue.

- Professional Services derives its revenue from (a) professional management services in the gaming industry through Butler National Service Corporation ("BNSC") and BHCMC, LLC ("BHCMC"), and (b) professional architectural, engineering and management support services. Revenue from Professional Services increased 5% for the three months to \$7.7 million at October 31, 2016 compared to \$7.3 million at October 31, 2015.
- Aerospace Products derives its revenue by designing, engineering, manufacturing, installing, servicing and repairing products for classic and current production aircraft. Aerospace Products revenue increased 84% for the three months to

\$5.1 million at October 31, 2016 compared to \$2.8 million at October 31, 2015. This increase is primarily due to an increase in avionics-related revenue of \$1.2 million and an increase of modification revenue of \$1.0 million. We anticipate future domestic military spending reductions and continued slow growth of the United States economy.

Costs and expenses:

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

Costs and expenses increased 9% in the three months ended October 31, 2016 to \$11.6 million compared to \$10.7 million in the three months ended October 31, 2015. Costs and expenses were 91% of total revenue in the three months ended October 31, 2016, as compared to 106% of total revenue in the three months ended October 31, 2015.

Costs of Professional Services increased by 2% in the three months ended October 31, 2016 to \$4.6 million compared to \$4.5 million in the three months ended October 31, 2015. Costs were 36% of total revenue in the three months ended October 31, 2016, as compared to 45% of total revenue in the three months ended October 31, 2015.

Costs of Aerospace Products increased by 51% in the three months ended October 31, 2016 to \$3.7 million compared to \$2.4 million for the three months ended October 31, 2015. Costs were 29% of total revenue in the three months ended October 31, 2016, as compared to 24% of total revenue in the three months ended October 31, 2015.

Marketing and advertising expenses decreased by 6% in the three months ended October 31, 2016, to \$1.1 million compared to \$1.1 million in the three months ended October 31, 2015. Expenses were 8% of total revenue in the three months ended October 31, 2016, as compared to 11% of total revenue in the three months ended October 31, 2015. Marketing and advertising expenses include advertising, sales and marketing labor, gaming development costs, and casino and product promotions.

Employee benefits expenses as a percent of total revenue was 4% in the three months ended October 31, 2016, compared to 4% in the three months ended October 31, 2015. These expenses increased 2% to \$438 in the three months ended October 31, 2016, from \$429 in the three months ended October 31, 2015. These expenses include the employers' share of all federal, state and local taxes, paid time off for vacation, holidays and illness, employee health and life insurance programs and employer matching contributions to retirement plans.

Depreciation and amortization expenses as a percent of total revenue was 4% in the three months ended October 31, 2016, compared to 6% in the three months ended October 31, 2015. These expenses decreased 10% to \$507 in the three months ended October 31, 2016, from \$566 in the three months ended October 31, 2015. These expenses include depreciation related to owned assets being depreciated over various useful lives and amortization of intangible items including the Kansas privilege fee related to the Boot Hill Casino being expensed over the term of the gaming contract with the State of Kansas. Phase II expansion to Boot Hill Casino was formally completed in early January 2013 and we began depreciation on \$4.9 million of assets with various useful lives. BHCMC, LLC depreciation and amortization expense for the three months ended October 31, 2016 was \$356 compared to \$337 in the three months ended October 31, 2015.

General, administrative and other expenses as a percent of total revenue was 10% in the three months ended October 31, 2016, compared to 16% in the three months ended October 31, 2015. These expenses decreased 18% to \$1.3 million in the three months ended October 31, 2016, from \$1.6 million in the three months ended October 31, 2015.

Other income (expense):

Other income (expense) was (\$105) in the three months ended October 31, 2016, compared with other income (expense) of (\$108) in the three months ended October 31, 2015. Interest related to obligations of BHCMC, LLC was \$53 in the three months ended October 31, 2016 compared to \$66 in the three months ended October 31, 2015.

Operations by Segment

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

The following table presents a summary of our operating segment information for the three months ended October 31, 2016 and October 31, 2015:

(dollars in thousands)	Three Months Ended <u>October 31, 2016</u>	Percent of Total Revenue	Three Months Ended <u>October 31, 2015</u>	Percent of Total Revenue	Percent Change <u>2015-2016</u>
Professional Services					
Revenue					
Boot Hill Casino	\$ 7,624	99%	\$ 7,147	97%	7%
Management/Professional Services	<u>98</u>	<u>1%</u>	<u>187</u>	<u>3%</u>	<u>(48)%</u>
Revenue	<u>7,722</u>	<u>100%</u>	<u>7,334</u>	<u>100%</u>	<u>5%</u>
Costs of Professional Services	4,649	60%	4,539	62%	2%
Expenses	<u>2,568</u>	<u>33%</u>	<u>2,763</u>	<u>38%</u>	<u>(7)%</u>
Total costs and expenses	<u>7,217</u>	<u>93%</u>	<u>7,302</u>	<u>100%</u>	<u>(1)%</u>
Professional Services operating income before noncontrolling interest in BHCMC, LLC	<u>\$ 505</u>	<u>7%</u>	<u>\$ 32</u>	<u>0%</u>	<u>1,478%</u>

(dollars in thousands)	Three Months Ended <u>October 31, 2016</u>	Percent of Total Revenue	Three Months Ended <u>October 31, 2015</u>	Percent of Total Revenue	Percent Change <u>2015-2016</u>
Aerospace Products					
Revenue	\$ 5,091	100%	\$ 2,772	100%	84%
Costs of Aerospace Products	3,698	73%	2,449	88%	51%
Expenses	<u>734</u>	<u>14%</u>	<u>954</u>	<u>35%</u>	<u>(23)%</u>
Total costs and expenses	<u>4,432</u>	<u>87%</u>	<u>3,403</u>	<u>123%</u>	<u>30%</u>
Aerospace Products operating income (loss)	<u>\$ 659</u>	<u>13%</u>	<u>\$ (631)</u>	<u>(23)%</u>	

Professional Services

- Revenue from Professional Services increased 5% for the three months ended October 31, 2016 to \$7.7 million compared to \$7.3 million for the three months ended October 31, 2015.

In the three months ended October 31, 2016 Boot Hill Casino received gross receipts for the State of Kansas of \$10.1 million compared to \$9.6 million for the three months ended October 31, 2015. Mandated fees, taxes and distributions reduced gross receipts by \$3.3 million resulting in gaming revenue of \$6.8 million for the three months ended October 31, 2016, compared to a reduction to gross receipts of \$3.2 million resulting in gaming revenue of \$6.4 million for the three months ended October 31, 2015. Non-gaming revenue at Boot Hill Casino increased to \$841 for the three months ended October 31, 2016, compared to \$793 for the three months ended October 31, 2015.

The remaining management and Professional Services revenue includes professional management services in the gaming industry, and licensed architectural services. Professional Services revenue excluding Boot Hill Casino decreased 48% to \$98 for the three months ended October 31, 2016, compared to \$187 for the three months ended October 31, 2015.

- Costs of Professional Services increased 2% in the three months ended October 31, 2016 to \$4.6 million compared to \$4.5 million in the three months ended October 31, 2015. Costs were 60% of segment total revenue in the three months ended October 31, 2016, as compared to 62% of segment total revenue in the three months ended October 31, 2015.
- Expenses decreased 7% in the three months ended October 31, 2016 to \$2.6 million compared to \$2.8 million in the three months ended October 31, 2015. Expenses were 33% of segment total revenue in the three months ended October 31, 2016, as compared to 38% of segment total revenue in the three months ended October 31, 2015.

Aerospace Products

- Revenue increased 84% to \$5.1 million in the three months ended October 31, 2016, compared to \$2.8 million in the three

months ended October 31, 2015. We anticipate future domestic military spending reductions and continued slow growth of the United States economy. In an effort to offset decreased domestic military spending, we have invested in the development of several STCs. These STCs are state of the art avionics and we are aggressively marketing both domestically and internationally.

- Costs of Aerospace Products increased by 51% in the three months ended October 31, 2016 to \$3.7 million compared to \$2.4 million for the three months ended October 31, 2015. Costs were 73% of segment total revenue in the three months ended October 31, 2016, as compared to 88% of segment total revenue in the three months ended October 31, 2015.
- Expenses decreased 23% in the three months ended October 31, 2016 to \$734 compared to \$1.0 million in the three months ended October 31, 2015. Expenses were 14% of segment total revenue in the three months ended October 31, 2016, as compared to 35% of segment total revenue in the three months ended October 31, 2015.

Employees

Other than persons employed by our gaming subsidiaries there were 83 full time and 2 part time employees on October 31, 2016, compared to 88 full time and 4 part time employees on October 31, 2015. As of December 9, 2016, staffing is 83 full time and 2 part time employees. Our staffing at Boot Hill Casino & Resort on October 31, 2016 was 182 full time and 65 part time employees compared to 182 full time and 53 part time employees on October 31, 2015. At December 9, 2016 there are 184 full time and 74 part time employees. None of the employees are subject to any collective bargaining agreements.

Liquidity and Capital Resources

We believe that our current banks will provide the necessary capital for our business operations. However, we continue to maintain contact with other banks that have an interest in funding our working capital needs to continue our growth in operations in fiscal 2017 and beyond.

The ownership structure of BHCMC, LLC is now:

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

Our wholly owned subsidiary, Butler National Service Corporation continues friendly discussions with the other member of BHCMC, LLC to explore the possible acquisition by Butler National Service Corporation of the other member's 20% equity interest in BHCMC, LLC. If and when a definitive agreement is reached, such definitive agreement and a press release concerning the acquisition will be issued to describe the terms of the agreement and the intentions of the members. We have not set a definitive timetable for our discussions and there can be no assurances that the process will result in any transaction being announced or completed. At present there is no disagreement between the members of BHCMC, LLC. We do not plan to disclose or comment on developments until further disclosure is deemed appropriate.

BHCMC, LLC, rents the casino building under the terms of a 25 year lease from BHC Development L.C. ("BHCD"). Butler National Service Corporation continues friendly discussions with BHC Development L.C. to explore the possible acquisition by Butler National Service Corporation of the casino building and related land. If and when a definitive agreement is reached, such definitive agreement and press release concerning the acquisition will be issued to describe the terms of the agreement and the intentions of the members. Butler National Corporation, its management, and its subsidiaries have no ownership interest in BHCI or BHCD.

Analysis and Discussion of Cash Flow

During the six months ended October 31, 2016 our cash position decreased by \$935. Net income was \$1.2 million for the six months ended October 31, 2016. Cash flows provided by operating activities was \$2.9 million for the six months ended October 31, 2016. Non-cash activities consisting of depreciation and amortization contributed \$1.8 million. Customer deposits increased our cash position by \$1.5 million while inventories increased our cash position by \$356. Accounts receivable decreased our cash position by \$1.7 million. Gaming facility mandated payments decreased our cash position by \$111. Prepaid expenses and other assets decreased our cash by \$116, while a decrease in accounts payable and a decrease in accrued expenses and other current liabilities decreased our cash by an additional \$568. Deferred tax assets increased our cash position by \$418.

Cash used in investing activities was \$911 for the six months ended October 31, 2016. We invested \$176 in an airplane, \$467 to purchase equipment and \$268 to develop and enhance STCs.

Cash used in financing activities was \$3.0 million for the six months ended October 31, 2016. We made repayments on our debt of \$1.4 million and decreased promissory notes by \$1.2 million. We made a distribution to our non-controlling member of \$360.

Critical Accounting Policies and Estimates:

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

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

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

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

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

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Future events and their effects cannot be determined with certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results could differ from those estimates, and any such differences may be material to our financial statements. Significant estimates include assumptions about collection of accounts receivable, the valuation and recognition of stock-based compensation expense, valuation for deferred tax assets and useful life of fixed assets.

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

Supplemental Type Certificates: Supplemental Type Certificates (STCs) are authorizations granted by the Federal Aviation Administration (FAA) for specific modification of a certain aircraft. The STC authorizes us to perform modifications, installations, and assemblies on applicable customer-owned aircraft. Costs incurred to obtain STCs are capitalized and subsequently amortized over a seven year life. The legal life of an STC is indefinite.

Changing Prices and Inflation

We have experienced upward pressure from inflation in fiscal year 2017. From fiscal year 2016 to fiscal year 2017 a majority of the increases we experienced were in material costs. This additional cost may not be transferable to our customers resulting in lower income in the future. We anticipate fuel costs and possibly interest rates to rise in fiscal 2017 and 2018.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are a smaller reporting Company as defined by Rule 12b-2 under the Securities Exchange Act of 1934, and are not required to provide the information required under this item.

Item 4. CONTROLS AND PROCEDURES

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

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

In connection with the preparation of this Form 10-Q, our Chief Executive Officer and our Chief Financial Officer conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of October 31, 2016. Based on that evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of October 31, 2016.

Internal Control Over Financial Reporting

Limitations on Controls

Our management, including the Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

Changes in Internal Control Over Financial Reporting: In our opinion there were no changes in the Company's internal control over financial reporting during the three months ended October 31, 2016 that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1.

LEGAL PROCEEDINGS.

As of December 9, 2016, there are no significant known legal proceedings pending against us. We consider all such unknown proceedings, if any, to be ordinary litigation incident to the character of the business. We believe that the resolution of any claims will not, individually or in the aggregate, have a material adverse effect on the financial position, results of operations, or liquidity of the Company.

Item 1A.

RISK FACTORS.

There are no material changes to the risk factors disclosed under Item 1A of our Form 10-K or to the Cautionary Statements filed by us as Exhibit 99 to the Form 10-K for the fiscal year ended April 30, 2016.

Item 2.

UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None.

Item 3.

DEFAULTS UPON SENIOR SECURITIES.

None.

Item 4.

MINE SAFETY DISCLOSURES.

Not applicable.

Item 5.

OTHER INFORMATION.

None.

Item 6.

EXHIBITS.

- 3.1 Articles of Incorporation, as amended and restated are incorporated by reference to Exhibit 3.1 of our Form DEF 14A filed on December 26, 2001.
- 3.2 Bylaws, as amended, are incorporated by reference to Exhibit 3.2 of our Form 10-Q filed on March 14, 2013.
- 4.1 Rights Agreement, dated August 2, 2011, by and between Butler National Corporation and UMB Bank, N.A., as Rights Agent, which includes the form of Certificate of Designations, setting forth the terms of the Series C Participating Preferred Stock, par value \$5.00 per share, as Exhibit A, the form of Right Certificate as Exhibit B and the summary of the rights as Exhibit C.
- 31.1 Certificate of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a).
- 31.2 Certificate of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a).
- 32.1 Certifications of Chief Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certifications of Chief Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 99.1 Cautionary Statements for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995, are incorporated by reference to Exhibit 99 of the Form 10-K for the fiscal year ended April 30, 2016.
- 99.2 Investor Presentation for the 2016 Annual Meeting of Shareholders of Butler National Corporation, which is incorporated by reference to Exhibit 99.1 of the Company's Current Report on Form 8-K dated November 8, 2016.
- 101 The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended October 31, 2016, formatted in XBRL (Extensible Business Reporting Language) includes: (i) Condensed Consolidated Balance Sheets as of October 31, 2016 and April 30, 2016, (ii) Condensed Consolidated Statements of Operations for the three months ended October 31, 2016 and 2015 and six months ended October 31, 2016 and 2015, (iii) Condensed Consolidated Statements of Cash Flows for the six months ended October 31, 2016 and 2015, and (iv) the Notes to Consolidated Financial Statements, with detail tagging.

SIGNATURES

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

BUTLER NATIONAL CORPORATION
(Registrant)

December 13, 2016
Date

/s/ Clark D. Stewart

Clark D. Stewart
(President and Chief Executive Officer)

December 13, 2016
Date

/s/ Craig D. Stewart

Craig D. Stewart
(Chief Financial Officer)

Exhibit Index

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