

BUTLER NATIONAL CORP
Form 10-Q
September 12, 2008

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 quarter ended **July 31, 2008**

Commission File Number **0-1678**

BUTLER NATIONAL CORPORATION

(Exact name of Registrant as specified in its charter)

Kansas

41-0834293

(State of Incorporation)

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

19920 West 161st Street, Olathe, Kansas 66062

(Address of Principal Executive Office)(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

Common Stock \$.01 Par Value

(Title of Class)

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 and (2) has been subject to such filing requirements for the past ninety days: 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 "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.:

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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 September 5, 2008 was **55,091,109** shares.

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES

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BUTLER NATIONAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

| ASSETS | <u>07/31/08</u> | <u>4/30/08</u> | LIABILITIES AND STOCKHOLDERS' EQUITY | <u>07/31/08</u> | <u>4/30/08</u> |
|-----------------|-----------------|----------------|---|-----------------|----------------|
| | (unaudited) | (audited) | | (unaudited) | (audited) |
| CURRENT ASSETS: | | | CURRENT LIABILITIES: | | |
| Cash | \$ 2,565,374 | \$ 2,969,715 | | \$ 171,129 | \$ 144,024 |

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| | | | | |
|---|------------|--|------------|------------|
| | | Bank overdraft payable | | |
| Accounts receivable, net of allowance for doubtful accounts of \$75,040 at July 31, 2008 and \$75,040 at April 30, 2008 | 972,336 | Promissory notes payable | 5,646,728 | 711,081 |
| | 1,289,898 | Current maturities of long-term debt and capital lease obligations | 4,587,346 | 4,643,567 |
| | | Accounts payable | 763,708 | 558,085 |
| | | Customer deposits | 1,678,097 | 1,417,503 |
| Inventories - | | Accrued liabilities | | |
| Raw materials | 5,229,348 | Compensation and compensated absences | 404,188 | 428,775 |
| Work in process | 501,080 | Accrued income tax | 149,000 | 324,643 |
| Finished goods | 2,170,226 | Other | 282,951 | 269,868 |
| Aircraft | 4,772,767 | | | |
| | | Total current liabilities | 13,683,147 | 8,497,546 |
| | ----- | | | |
| | 12,673,421 | LONG-TERM DEBT AND CAPITAL LEASE, NET | | |
| | 12,408,109 | OF CURRENT MATURITIES | 6,272,207 | 6,416,184 |
| | | | | |
| Prepaid expenses and other current assets | 5,698,370 | | | |
| | 207,419 | | | |
| | ----- | | | |
| Total current assets | 21,909,501 | Total liabilities | 19,955,354 | 14,913,730 |
| | 16,875,141 | | | |

COMMITMENTS AND CONTINGENCIES
STOCKHOLDERS' EQUITY:

PROPERTY, PLANT AND EQUIPMENT:

| | | | | |
|-------------------------------|------------|---|--|--|
| Land and building | 4,577,064 | Preferred stock, par value \$5 | | |
| | 44,216,320 | Authorized 50,000,000 shares, all classes | | |
| Machinery and equipment | 2,069,332 | Designated Classes A and B, 200,000 shares | | |
| | 2,069,332 | \$1,000 Class A, 9.8%, cumulative if earned | | |
| Office furniture and fixtures | 808,489 | | | |
| | 802,127 | | | |
| Leasehold improvements | 4,249 | | | |
| | 4,249 | | | |

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| | | | | | |
|--|---------------|---------------|--|--------------|---------------|
| | ----- | | liquidation and redemption value \$100, | | |
| | 7,459,134 | 7,092,028 | no shares issued and outstanding | - | - |
| Accumulated depreciation | (2,426,566) | (2,385,105) | \$1,000 Class B, 6%, convertible cumulative, | | |
| | ----- | | liquidation and redemption value \$1,000 | | |
| | 5,032,571 | 4,706,923 | no shares issued and outstanding | - | - |
| SUPPLEMENTAL TYPE CERTIFICATES | 2,057,019 | 2,057,019 | Common stock, par value \$.01: | | |
| | | | Authorized 100,000,000 shares issued and outstanding | | |
| | | | 55,091,109 shares at | | |
| | | | at July 31 and | 550,911 | 550,911 |
| | | | 55,091,109 at April 30, 2008 | | |
| ADVANCES FOR GAMING DEVELOPMENTS | | | Common stock, owed but not issued 278,573 shares | | |
| (net of reserves of \$3,425,640 at 7/31/08 and \$3,346,623 at 4/30/08) | 1,806,551 | 1,806,551 | at July 31 and | 2,786 | 2,786 |
| | | | 278,573 at April 30, 2008 | | |
| | | | Capital contributed in excess of par | 11,076,238 | 11,076,238 |
| | | | Treasury stock at cost (600,000 shares) | (732,000) | (732,000) |
| OTHER ASSETS | 1,658,224 | 1,658,224 | Retained earnings | 1,610,577 | 1,292,193 |
| | | | | ----- | ----- |
| | | | Total stockholders' equity | 12,508,512 | 12,190,128 |
| | | | | ----- | ----- |
| Total assets | \$ 32,463,866 | \$ 27,103,858 | Total liabilities and stockholders' equity | \$ 2,463,866 | \$ 27,103,858 |
| | ===== | | | ===== | ===== |

The accompanying notes are an integral part of these financial statements

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED INCOME STATEMENT

| | THREE MONTHS ENDED | |
|--|--------------------|--------------|
| | July 31, | |
| | <u>2008</u> | <u>2007</u> |
| | (unaudited) | (unaudited) |
| REVENUES | | |
| Aircraft / Modifications | \$ 3,447,130 | \$ 1,894,679 |
| Avionics / Defense | 871,249 | 1,659,311 |
| Management / Professional Services | 885,743 | 1,153,338 |
| | ----- | ----- |
| Net Revenues | 5,204,122 | 4,707,328 |
| COST OF SALES | | |
| Aircraft / Modifications | 2,455,315 | 1,636,587 |
| Avionics / Defense | 725,667 | 946,738 |
| Management / Professional Services | 281,946 | 599,562 |
| | ----- | ----- |
| Total Cost of Sales | 3,462,928 | 3,182,887 |
| | ----- | ----- |
| GROSS PROFIT | 1,741,194 | 1,524,441 |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 1,085,144 | 1,114,216 |
| | ----- | ----- |

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| | | |
|---|------------|------------|
| OPERATING INCOME | 656,050 | 410,225 |
| OTHER INCOME (EXPENSE) | | |
| Interest expense | (231,036) | (132,639) |
| Other | 2,475 | - |
| | ----- | ----- |
| Other expense | (228,561) | (132,639) |
| INCOME (LOSS) BEFORE PROVISION FOR INCOME TAXES | 427,489 | 277,586 |
| PROVISION FOR INCOME TAXES | (109,105) | (45,747) |
| | ----- | ----- |
| NET INCOME (LOSS) | \$ 318,384 | \$ 231,839 |
| | ===== | ===== |
| | | |
| BASIC EARNINGS PER COMMON SHARE | \$.01 | \$.00 |
| | ===== | ===== |
| Shares used in per share calculation | 54,769,682 | 53,245,642 |
| | ===== | ===== |
| DILUTED EARNINGS PER COMMON SHARE | \$.01 | \$.00 |
| | ===== | ===== |
| Shares used in per share calculation | 54,899,086 | 53,358,984 |
| | ===== | ===== |

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

THREE MONTHS ENDED

July 31,

2008

2007

(unaudited)

(unaudited)

CASH FLOWS FROM OPERATING
ACTIVITIES

| | | | | |
|---|----|-------------|----|-----------|
| Net income (loss) | \$ | 318,384 | \$ | 231,839 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operations - | | | | |
| Depreciation | | 41,458 | | 37,160 |
| Changes in assets and liabilities: | | | | |
| Accounts receivable | | 317,562 | | 218,298 |
| Contracts in process | | - | | (350,684) |
| Inventories | | (265,312) | | 476,288 |
| Prepaid expenses and other current assets | | (5,490,951) | | (407) |
| Accounts payable | | 232,728 | | (69,258) |
| Customer deposits | | 260,594 | | (513,020) |

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| | | |
|--|------------------|------------------|
| Accrued liabilities | (187,147) | 105,102 |
| | ----- | ----- |
| Cash provided by (used in) operating activities | (4,772,684) | 135,318 |
| | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Capital expenditures - Property, Plant & Equipment | (367,106) | (22,666) |
| | ----- | ----- |
| Cash provided by (used in) investing activities | (367,106) | (22,666) |
| | | |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Borrowings under promissory notes, net | 4,935,647 | (507,211) |
| Repayments of long-term debt | (200,198) | 185,047 |
| | ----- | ----- |
| Cash provided by (used in) financing activities | 4,735,449 | (322,164) |
| | ----- | ----- |
| NET INCREASE (DECREASE) IN CASH | (404,341) | (209,512) |
| | | |
| CASH, beginning of period | 2,969,715 | 1,789,169 |
| | ----- | ----- |
| CASH, end of period | \$ 2,565,374 | \$ 1,579,657 |
| | ===== | ===== |

SUPPLEMENTAL DISCLOSURES OF
CASH FLOW INFORMATION

| | | | | |
|-------------------|----|---------|----|---------|
| Interest paid | \$ | 208,743 | \$ | 132,639 |
| Income taxes paid | | 284,748 | | 15,747 |

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

BUTLER NATIONAL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q 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 dated April 30, 2008. In our opinion, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation have been included. Operating results for the three months ended July 31, 2008 are not indicative of the results of operations that may be expected for the year ending April 30, 2009.

Certain reclassifications within the condensed financial statement captions have been made to maintain consistency in presentation between years.

2.

Advances for Gaming Developments: We are advancing funds for the establishment of gaming. These funds have been capitalized in accordance with Statements of Financial Accounting Standards (SFAS) 67 "Accounting for Costs and Initial Rental Operations of Real Estate Projects." Such standard requires costs associated with the acquisition, development, and construction of real estate and real estate-related projects to be capitalized as part of that project.

Our advances represent costs to be reimbursed upon approval of gaming in several locations. We have agreements in place which require payments to be made to us for the respective projects upon opening of Indian gaming facilities. Once gaming facilities have gained proper approvals, we plan to enter into a note receivable arrangement with the Tribe to secure reimbursement of advanced funds for that particular project.

We have advanced and invested a total of \$5,232,191 at July 31, 2008 and \$5,153,174 at April 30, 2008 in gaming developments. We have reserves of \$3,425,640, at July 31, 2008 and \$3,346,623 at April 30, 2008. We believe that our advances for gaming developments will be totally reimbursed as casinos are opened. We believe it is necessary to establish reserves against the advances because all of the proposed casinos are involved in legal and governmental actions whose outcome is not certain nor is there any time frame for resolution. The reserve amount is an estimate of the value we would receive if a casino was not opened and we were forced to liquidate the assets that we have acquired with our advances. These assets were intended to be used with casinos and consist of the purchase of land and land improvements related to the development of Gaming facilities. We believe that these tracts could be developed and sold for residential and commercial use to recover our advances if the gaming enterprises do not open.

In fiscal year 2008 we added a reserve of approximately \$434,000 for the proposed Dodge City gaming developments. We had an additional reserve of approximately \$79,000 in the quarter ending July 31, 2008. We review quarterly the amount of any increase in reserves based on our determination of the fair value of assets acquired by our advances for gaming developments.

3. Entertainment Development: We had land development purchases totaling \$360,744 and expenses of

approximately \$206,829 during the three months ending July 31, 2008. Net borrowings at July 31, 2008 towards the purchase of land were \$1,370,837.

4. Earnings Per Share: Earnings per common share are based on the weighted average number of common shares outstanding during the year. Stock options have been considered in the dilutive earnings per share calculation.

5. Research and Development: We invested in research and development activities. The amount invested in the three months ended July 31, 2008 and 2007 was approximately \$1,061,000 and \$569,500 respectively. We charge to operations research and development costs. The amount charged in the three months ended July 31, 2008 and 2007 was approximately \$620,000 and \$545,600 respectively.

6. Borrowings: Two promissory notes were entered into during the quarter ended July 31, 2008 totaling \$5,500,000. These notes were for a privilege fee to the State of Kansas in connection with our application to be the manager of the State owned casino in Ford County, Kansas. The deposit should be returned to us if we are not the successful applicant for the Southwest Gaming Zone. If we are the selected applicant, the deposit is the payment of the privilege fee to the State of Kansas.

A line of credit in the amount of \$1,224,285 was entered into on July 7, 2006. An additional line of credit in the amount of \$1,508,000 was entered into on October 25, 2006. Both lines of credit are to be used for the BCS Design, Inc. construction projects in Junction City, Kansas. As of July 31, 2008 our current borrowings are \$924,471 and \$1,053,646 respectively. These notes have been renewed bi-annually during the past 12 months.

7. Subsequent Events: We have signed real estate contracts for the sale of three homes in Junction City, Kansas since July 31, 2008. We expect these contracts to close during the second quarter of fiscal year 2009.

Butler National Service Corporation, a wholly owned subsidiary of Butler National Corporation, signed an Amended and Restated Limited Liability Company agreement in connection with a Butler National affiliate providing services in connection with the State of Kansas' ownership and operation of a proposed Lottery Gaming Facility in Dodge City, Kansas.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

RISK FACTORS

The information set forth below includes "forward-looking" information and is subject to Risk Factors as outlined in the Private Securities Litigation Reform Act of 1995. The Risk Factors listed under Item 1A of our Form 10-K and the Cautionary Statements, filed by us as Exhibit 99 to our Form 10-K, are incorporated herein by reference and you are specifically referred to such Risk Factors and Cautionary Statements for a discussion of factors which could affect our operations and forward-looking statements contained herein.

RESULTS OF OPERATIONS

FIRST QUARTER FISCAL 2009 COMPARED TO FIRST QUARTER FISCAL 2008

Our sales for the three months ended July 31, 2008 were \$5,204,122, an increase of 10.6% from the three months ended July 31, 2007 with sales of \$4,707,328. Our operating profit for the three months ended July 31, 2008 was \$656,050, compared to \$410,225 for the three months ended July 31, 2007, an increase of 60%.

Discussion of the specific changes by operation at each business segment follows:

Aircraft Modifications: Sales from Aircraft Modifications including modified aircraft increased 81.9% from \$1,894,679 in the first three months of fiscal year 2008 to \$3,447,130 in the current three months of fiscal 2009. The modifications segment had an operating profit of \$774,867 in the three months ended July 31, 2008, compared to a profit of \$112,972 in the three months ended July 31, 2007. Avcon RVSM sales decreased by approximately \$35,936. Revenues generated from other modification services increased \$1,211,388 in the three months ended July 31, 2008.

During the past few years we have seen a significant increase in aircraft camera modification. Several custom engineering projects and aircraft modifications have also attributed to our increase in sales. As the economy grows aircraft owners may elect to update, modify, and purchase business aircraft. A shift to business aircraft ownership positively impacts our aircraft modification revenues. Although we cannot anticipate the future we must always consider the negative impact of items such as the September 11, 2001 event, increases in fuel prices, and general economic downturns.

Aircraft Acquisitions and Sales: There was no activity in the three months ended July 31, 2008 or in the three months ended July 31, 2007. We acquired no aircraft during the three months ended July 31, 2008. Management expects this business segment to have increased sales in the next year. FAA required modifications to the business aircraft fleet may increase customer demand for company owned aircraft.

Avionics: Sales from Avionics decreased 45.7%, from \$1,659,311 in the three months ended July 31, 2007, to \$871,249 in the three months ended July 31, 2008. Operating profits decreased from \$516,259 for the three months ended July 31, 2007 to a loss of \$41,106 for the three months ended July 31, 2008. The decrease in operating profit is related to additional material cost, material spoilage, additional labor requirements and rework labor costs on a major build-to-print contract. This contract was started in fiscal 2007 and is expected to be completed during the next quarter with less of an impact on operating profit. Management expects this business segment to increase in the future due to additions of

new fuel system protection devices like the TSD, GFI, and other classic aviation defense products.

Services - SCADA Systems and Monitoring Services: Revenue decreased from \$471,610 for the three months ended July 31, 2007 to \$381,059 for the three months ended July 31, 2008, a decrease of 19.2%. During the three months ended July 31, 2008 we maintained a relatively level volume of long-term contracts with municipalities. We had decreased revenues due to budget cuts faced by the municipalities resulting from the decrease in property taxes in the State of Florida. We anticipate the revenues from additional lift station rehabilitations to resume and generate additional revenue over the next four years. Revenue fluctuates due to the

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introduction of new products and services and the related installations of these types of products. Our contracts with our two largest customers have been renewed through fiscal 2009.

Gaming: Revenues from management services related to gaming increased 13.9% from \$351,277 for the three months ended July 31, 2007 compared to \$400,089 for the three months ended July 31, 2008. Sales continue to have stability due to the addition of Class III casino gaming in Oklahoma.

Corporate / Professional Services:

These services include the architectural services of BCS Design, Inc., arrangements for financing, on site contract management of gaming establishments, flight, and engineering services. Management consulting and professional fees, including sales related to completed projects, were \$119,747 for the three months ended July 31, 2008 and \$330,451 for three months ended July 31, 2007, a decrease of 68.3%. Sales related to construction projects were approximately \$168,000 at July 31, 2007 and zero at July 31, 2008.

Selling, General and Administrative (SG&A): Expenses were \$1,085,144, 20.8% of revenues, for the three months ended July 31, 2008 compared to 23.6% of revenues for the three months ending July 31, 2007. Business overhead expenses were decreased overall due to a reduction in cost towards our Kansas entertainment endeavors.

Other Income (Expense):

Other interest increased from \$132,639 in the three months ended July 31, 2007 to \$231,036 for the three months ended July 31, 2008.

Earnings: Our operating profit for the three months ended July 31, 2008 was \$656,050, compared to \$410,225 for the three months ended July 31, 2007, an increase of 60%. Our net income for the prior three months period ended July 31, 2007 was \$231,839. Our net income for the current three months ended July 31, 2008 was \$318,384.

Employees: We employed 92 at July 31, 2008 and 88 at July 31, 2007.

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 2009 and beyond.

Other than obligations related to the potential management of a gaming facility in Dodge City, Kansas and the purchase of the JET product line we do not, as of July 31, 2008, have any material commitments for other capital expenditures other than the terms of the Indian Management Agreements should any additional casinos be authorized. We will need additional funds to complete our planned Indian gaming opportunities. We will use current cash available as well as additional funds, for the start up and construction of gaming facilities. During the quarter ended July 31, 2008 we entered into two short term promissory notes totaling \$5,500,000 towards the privilege fee for the gaming facility in Ford county, Kansas. The deposit should be returned to us if we are not the successful applicant for the Southwest Gaming Zone. If we are the selected applicant, the deposit is the payment of the privilege fee to the State of Kansas. We anticipate initially obtaining these funds from internally generated working capital and borrowings.

Analysis and Discussion of Cash Flow

During the first quarter of fiscal year 2009 our cash position decreased by \$404,341 and can be attributed to the following. Cash used in operation activities was \$4,772,684. During the first quarter we made a large deposit of \$5,500,000 as a Privilege Fee to the Kansas Lottery as part of our gaming application for Ford

County. This deposit will be refunded if we are not selected as the Manager. During the first quarter of fiscal 2009 we reported net income of \$318,384. Other cash provided by operating activities included a decrease in Accounts receivable of \$317,562 and an increase in customer deposits of \$260,594. Accounts payable and accrued liabilities resulted in a net contribution of approximately \$45,500. Inventory increase by more than \$265,000 due to several large aircraft modification projects.

We invested approximately \$360,000 towards the development of the land purchased in Dodge City and less than \$10,000 for the addition of new equipment.

Cash provided by financing activities contributed a net of \$4,735,449. We had short term borrowing of \$5,500,000 for the Privilege Fee as part of our gaming application for Ford County. The deposit should be returned to us if we are not the successful applicant for the Southwest Gaming Zone. If we are the selected applicant, the deposit is the payment of the privilege fee to the State of Kansas. We reduced our promissory notes by \$564,352 and all other borrowing by \$200,198.

Critical Accounting Policies

Revenue Recognition: We perform aircraft modifications under fixed-price contracts. Revenues from fixed-price contracts are recognized on the percentage-of-completion method, measured by the direct labor costs incurred compared to total estimated direct labor costs. Revenue for off-the-shelf items and aircraft sales is recognized on the date of sale.

Revenue from Avionics are recognized when shipped and payment for materials are due within 30 days of invoicing. Revenue for SCADA services, Gaming Management, and other Corporate/Professional Services are recognized on a monthly basis as services are rendered. Payments for these services are usually received within 30 days of invoicing.

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 and have been accepted by the customers. In the rare event of a warranty claim, the claim is processed through the normal course of business; this may include additional charges to the customer. In our opinion any future warranty work would not be material to the financial statements.

Allowance for Doubtful Accounts: Allowance for doubtful accounts are calculated on the historical write-off of doubtful accounts of the individual subsidiaries. Invoices are generally considered a doubtful account if no payment has been made in the past 90 days. We review these policies on a quarterly basis, and based on these reviews, we believe we maintain adequate reserves.

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 revenues 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.

Impairment of Goodwill, Other Intangible Assets and Long-lived Assets: We comply with the provisions of Statement of Financial Standards No. 142, Goodwill and Other Intangible Assets (SFAS No. 142), which requires that we evaluate our goodwill and other assets for impairment at least annually or whenever events or circumstances indicate the carrying value of that asset may not be recoverable. Impairment is measured by comparing the carrying value of the long-lived asset to the estimated undiscounted future cash flows expected to result from the use of the assets and their eventual disposition. We determined that as of April 30, 2008 an impairment of \$302,537 was necessary.

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

Advances for Gaming Developments: We are advancing funds for the establishment of gaming. These funds have been capitalized in accordance with Statements of Financial Accounting Standards (SFAS) 67 "Accounting for Costs and Initial Rental Operations of Real Estate Projects." Such standard requires costs associated with the acquisition, development, and construction of real estate and real estate-related projects to be capitalized as part of that project.

Our advances represent costs to be reimbursed upon approval of gaming in several locations. We have agreements in place which require payments to be made to us for the respective projects upon opening of Indian gaming facilities. Once gaming facilities have gained proper approvals, we plan to enter into a note receivable arrangement with the Tribe to secure reimbursement of advanced funds for that particular project.

We have advanced and invested a total of \$5,232,191 at July 31, 2008 and \$5,153,174 at April 30, 2008 in gaming developments. We have reserves of \$3,425,640, at July 31, 2008 and \$3,346,623 at April 30, 2008. We believe that our advances for gaming developments will be totally reimbursed as casinos are opened. We believe it is necessary to establish reserves against the advances because all of the proposed casinos are involved in legal and governmental actions whose outcome is not certain nor is there any time frame for resolution. The reserve amount is an estimate of the value we would receive if a casino was not opened and we were forced to liquidate the assets that we have acquired with our advances. These assets were intended to be used with casinos and consist of the purchase of land and land improvements related to the development of Gaming facilities. We believe that these tracts could be developed and sold for residential and commercial use to recover our advances if the gaming enterprises do not open.

In fiscal year 2008 we added a reserve of approximately \$434,000 for the proposed Dodge City gaming developments. We had an additional reserve of approximately \$79,000 in the quarter ending July 31, 2008. We determine annually the amount of any increase in reserves based on our determination of the fair value of assets acquired by our advances for gaming developments.

Changing Prices and Inflation

We did experience some pressure from inflation in fiscal 2009. These include increases in airplane travel, fuel, material, and transportation costs. This additional cost may not be transferable to our customers resulting in lower income. We anticipate long-term fuel costs and possibly interest rates to rise in fiscal 2009 and 2010.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Part I Item 3:

Quantitative and Qualitative Disclosures about Market Risk.

None.

Part I Item 4:

Controls and Procedures

We maintain a set of disclosure controls and procedures designed to ensure that information required to be disclosed in our filings under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's 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 Quarterly Report on Form 10-Q and have determined that such disclosure controls and procedures are effective.

No change in the Company's internal control over financial reporting occurred during the fiscal quarter ended July 31, 2008 that has

Section 906 of the Sarbanes-Oxley Act of 2002.

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Exhibit Number 99

Cautionary Statements for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995, are incorporated by reference to Exhibit 99 of the Form 10-K for the fiscal year ended April 30, 2008.

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)

September 13, 2008
Date

/S/ Clark D. Stewart
Clark D. Stewart
(President and Chief Executive Officer)

September 13, 2008
Date

/S/ Angela D. Shinabargar
Angela D. Shinabargar
(Chief Financial Officer)