BALLANTYNE OF OMAHA INC
Form 10-Q
August 11, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2008

OR

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

For the transition period from to

Commission File Number: 1-13906

BALLANTYNE OF OMAHA, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**47-0587703** (IRS Employer Identification Number)
4350 McKinley Street, Omaha, Nebraska (Address of Principal Executive Offices)	**68112** Zip Code

(402) 453-4444

Registrant s telephone number, including area code:

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 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 x No o

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practicable date:

Class	**Outstanding as of August 9, 2008**
Common Stock, $.01, par value	14,001,063 shares

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Part I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statement

Ballantyne of Omaha, Inc. and Subsidiaries
Consolidated Balance Sheets
June 30, 2008 and December 31, 2007

	June 30, 2008 (Unaudited)	December 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	$ 4,864,083	$ 4,220,355
Restricted cash	1,194,229	1,191,747
Short-term investments		13,000,000
Accounts receivable (less allowance for doubtful accounts of $555,784 in 2008 and $534,526 in 2007)	7,850,192	7,841,348
Inventories, net	11,581,763	9,883,555
Recoverable income taxes	1,795,774	1,365,530
Deferred income taxes	2,035,450	1,695,926
Consignment inventory	311,808	2,767,899
Other current assets	654,128	322,102
Total current assets	30,287,427	42,288,462
Investment in securities	10,828,655	
Investment in Digital Link II joint venture	3,447,499	3,727,485
Property, plant and equipment, net	3,664,381	3,633,124
Goodwill	2,392,882	2,420,993
Intangible assets, net	1,781,002	2,047,185
Other assets	32,952	23,099
Total assets	$ 52,434,798	$ 54,140,348
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 5,418,437	$ 6,134,703
Warranty reserves	347,571	381,710
Accrued group health insurance claims	273,915	201,687
Accrued bonuses	156,874	54,178
Other accrued expenses	2,146,856	2,151,413
Customer deposits	951,069	974,910
Total current liabilities	9,294,722	9,898,601
Deferred income taxes	112,466	98,532
Other accrued expenses, net of current portion	1,231,882	1,101,517
Total liabilities	10,639,070	11,098,650
Stockholders equity:		
Preferred stock, par value $.01 per share; Authorized 1,000,000 shares, none outstanding		
Common stock, par value $.01 per share; Authorized 25,000,000 shares; issued 16,098,868 shares in 2008 and 15,956,243 in 2007	160,988	159,562
Additional paid-in capital	34,840,024	34,637,868
Accumulated other comprehensive income (loss):		
Foreign currency translation adjustment	(188,117)	(59,427)
Pension liability adjustment	75,833	75,833
Unrealized loss on investments in securities	(946,345)	
Retained earnings	23,168,799	23,543,316
	57,111,182	58,357,152
Less 2,097,805 common shares in treasury, at cost	(15,315,454)	(15,315,454)
Total stockholders equity	41,795,728	43,041,698
Total liabilities and stockholders equity	$ 52,434,798	$ 54,140,348

See accompanying notes to the condensed consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries
Consolidated Statements of Operations
Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Net revenues	$ 13,643,104	$ 12,659,994	$ 27,840,276	$ 25,590,744
Cost of revenues	11,593,249	10,177,781	23,480,540	20,386,747
Gross profit	2,049,855	2,482,213	4,359,736	5,203,997
Selling and administrative expenses:				
Selling	742,718	709,736	1,530,520	1,492,352
Administrative	1,634,972	1,594,003	3,660,268	3,027,050
Goodwill impairment		639,466		639,466
Total selling and administrative expenses	2,377,690	2,943,205	5,190,788	5,158,868
Gain on the transfer of assets		1,230		234,557
Gain on the sale of a assets	258,170		258,170	
Loss on disposal of fixed assets			(1,285)	(11,004)
Income (loss) from operations	(69,665)	(459,762)	(574,167)	268,682
Interest income	129,350	206,930	275,536	425,243
Interest expense	(9,163)	(8,897)	(17,698)	(19,154)
Equity in loss of joint venture	(184,909)	(73,380)	(297,900)	(73,380)
Other income (expense), net	19,882	(24,731)	46,674	(72,752)
Income (loss) before income taxes	(114,505)	(359,840)	(567,555)	528,639
Income tax benefit (expense)	(5,576)	162,674	193,038	(153,066)
Net income (loss)	$ (120,081)	$ (197,166)	$ (374,517)	$ 375,573
Basic earnings (loss) per share	$ (0.01)	$ (0.01)	$ (0.03)	$ 0.03
Diluted earnings (loss) per share	$ (0.01)	$ (0.01)	$ (0.03)	$ 0.03
Weighted average shares outstanding:				
Basic	13,890,882	13,813,048	13,874,661	13,789,603
Diluted	13,890,882	13,813,048	13,874,661	14,081,439

See accompanying notes to the condensed consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Six Months Ended June 30, 2008 and 2007
(Unaudited)

	2008	2007
Cash flows from operating activities:		
Net income (loss)	$ (374,517)	$ 375,573
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Provision for doubtful accounts	26,680	47,500
Provision for obsolete inventory	336,069	420,176
Depreciation of consignment inventory	593,625	544,643
Depreciation of property, plant, and equipment	451,900	536,521
Amortization of intangibles	220,076	44,251
Equity in loss of joint venture	297,900	73,380
Goodwill impairment		639,466
Loss on disposal of fixed assets	1,285	11,004
Gain on sale of assets	(258,170)	
Deferred income taxes	(306,424)	(644,440)
Share-based compensation expense	75,022	54,067
Excess tax benefits from stock options exercised	(92,362)	(124,321)
Changes in assets and liabilities:		
Accounts receivable	146,607	606,149
Inventories	(2,074,911)	(5,266,026)
Consignment inventory	1,862,466	(268,354)
Other current assets	(264,799)	(11,145)
Accounts payable	(952,077)	940,570
Warranty reserves	(33,778)	(100,851)
Accrued group health insurance claims	72,228	(48,337)
Accrued bonus	102,696	146,184
Other accrued expenses	60,091	(328,726)
Customer deposits	(22,177)	229,087
Current income taxes	(305,425)	(115,414)
Other assets	(1,850)	7,300
Net cash used in operating activities	(439,845)	(2,231,743)
Cash flows from investing activities:		
Increase in acquisition costs	(46,969)	(183,364)
Investment in joint venture	(17,914)	(276,755)
Proceeds from sale of assets	271,360	
Increase in restricted investments	(2,482)	(4,483)
Capital expenditures	(492,115)	(206,778)
Proceeds from sales of investment securities	1,225,000	2,500,000
Net cash provided by investing activities	936,880	1,828,620
Cash flows from financing activities:		
Payments on long-term debt		(14,608)
Proceeds from exercise of stock options	59,113	54,311
Excess tax benefits from stock options exercised	92,362	124,321
Net cash provided by financing activities	151,475	164,024
Effect of exchange rate changes on cash and cash equivalents	(4,782)	
Net increase (decrease) in cash and cash equivalents	643,728	(239,099)
Cash and cash equivalents at beginning of year	4,220,355	2,622,654
Cash and cash equivalents at end of year	$ 4,864,083	$ 2,383,555

See accompanying notes to the condensed consolidated financial statements.

Ballantyne of Omaha, Inc. and Subsidiaries
Notes to the Condensed Consolidated Financial Statements
Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

1. Nature of Operations

Ballantyne of Omaha, Inc., a Delaware corporation (Ballantyne or the Company), and its wholly-owned subsidiaries Strong Westrex, Inc., Strong Technical Services, Inc., and Strong Digital Systems, Inc., design, develop, manufacture, service and distribute theatre and lighting systems. The Company s products are distributed to movie exhibition companies, sports arenas, auditoriums, amusement parks and special venues.

2. Summary of Significant Accounting Policies

Basis of Presentation

The condensed consolidated financial statements included herein are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America for annual reporting purposes or those made in the Company s annual Form 10-K filing. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Form 10-K for fiscal 2007.

In the opinion of management, the unaudited condensed consolidated financial statements of the Company reflect all adjustments of a normal recurring nature necessary to present a fair statement of the financial position and the results of operations and cash flows for the respective interim periods. The results for interim periods are not necessarily indicative of trends or results expected for a full year. All significant intercompany balances and transactions have been eliminated in consolidation.

The preparation of condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results and changes in facts and circumstances may alter such estimates and affect results of operations and financial position in future periods. Certain amounts in the accompanying condensed consolidated financial statements and notes thereto have been reclassified to conform to the 2008 presentation.

Revenue Recognition

Ballantyne manufactures and sells motion picture projectors which are highly complex and have many components that make up a complete system, which is referred to as an integrated system. Each customer selects options for certain components that they select in determining the integrated system they chose to purchase. To recognize revenue, the Company follows the requirements of Staff Accounting Bulletin 104, *Revenue Recognition*, which consists of performing the following:

- Persuasive evidence of an arrangement exists
- Delivery has occurred or services have been rendered
- The seller s price to the buyer is fixed or determinable
- Collectibility is reasonably assured

Once the customer has determined the features for their integrated system, the Company manufactures the system to their preference and then ships the system when it is complete. Revenue is generally recognized upon shipment of the product to the third party. In those limited situations where the shipping terms are FOB destination point, the Company recognizes revenue when the product is delivered.

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Ballantyne of Omaha, Inc. and Subsidiaries
Notes to the Condensed Consolidated Financial Statements
Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

Consignment Inventory

Digital and film projection equipment is provided to potential customers for consignment and demonstration purposes under customer use agreements. Additionally, during 2007, the Company entered into operating lease agreements with third party customers for the use of the projection equipment of which a majority of the projection equipment was sold during the first quarter of 2008. The Company recognized revenue in accordance with Staff Accounting Bulletin 104, *Revenue Recognition*, upon delivery of title to customer. No other income was generated under these operating lease agreements. The Company considered the guidance contained within ARB 43, EITF 01-08 and SFAS No. 13 to determine the proper accounting treatment for the agreements referenced above.

Consignment inventory is reviewed for impairment by comparing the inventory to estimated future usage and sales. Digital and film projection equipment on consignment amounted to approximately $0.3 million and $2.8 million at June 30, 2008 and December 31, 2007, respectively.

Recently Issued Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS No. 141(R)). SFAS No. 141(R) establishes principles and requirements for how an acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree and the goodwill acquired. SFAS No. 141(R) also establishes disclosures requirements to enable the evaluation of the nature and financial effects of the business combination. The provisions of SFAS No. 141(R) will be effective for the Company s business combinations occurring on or after January 1, 2009. Management is currently assessing the effect of this pronouncement on the Company s consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* (SFAS No. 162). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles in the United States (GAAP). SFAS No. 162 will be effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board s related amendments to remove the GAAP hierarchy from auditing standards. The Company does not believe the adoption will have a material impact on its consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position No. FAS 142-3, *Determination of the Useful Life of Intangible Assets* (FSP No. FAS 142-3). FSP No. FAS 142-3 requires companies estimating the useful life of a recognized intangible asset to consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, to consider assumptions that market participants would use about renewal or extension as adjusted for SFAS No. 142 s, *Goodwill and Other Intangible Assets,* entity-specific factors. FSP No. FAS 142-3 will be effective for the Company beginning in the first quarter of its fiscal year 2010. Management is currently assessing the effect of this pronouncement on the Company s consolidated financial statements.

3. Investment in Digital Link II Joint Venture

On March 6, 2007, the Company entered into an agreement with RealD to form an operating entity, Digital Link II, LLC (the LLC). Under the agreement, the LLC was formed with the Company and RealD as the only two members with membership interests of 44.4% and 55.6%, respectively. The LLC was formed for purposes of commercializing certain 3D technology and to fund the deployment of digital projector systems and servers to exhibitors. As of June 30, 2008, total current and non-current assets of the joint venture amounted to approximately $1.0 million and $8.6 million, respectively. Total liabilities and equity at June 30, 2008 amounted to $1.5 million and $8.1 million, respectively. The joint venture, which operates on a fiscal year end of March 31, 2008, reported a net loss for the three months ended June 30, 2008 of approximately $0.3 million which primarily resulted from depreciation expense related to projection equipment on consignment to third party customers.

Ballantyne of Omaha, Inc. and Subsidiaries
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The Company accounts for its investment by the equity method. Under this method, the Company records its proportionate share of Digital Link II s net income or loss based on the most recently available financial statements. The Company s portion of losses of the LLC amounted to approximately $0.3 million for the six months ended June 30, 2008.

4. Earnings (Loss) Per Common Share

The Company computes and presents earnings (loss) per share in accordance with SFAS No. 128, *Earnings Per Share*. Basic earnings (loss) per share has been computed on the basis of the weighted average number of shares of common stock outstanding. Diluted earnings (loss) per share has been computed on the basis of the weighted average number of shares of common stock outstanding after giving effect to potential common shares from dilutive stock options. The following table provides a reconciliation between basic and diluted income (loss) per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Basic earnings (loss) per share:				
Income (loss) applicable to common stock	$ (120,081)	$ (197,166)	$ (374,517)	$ 375,573
Weighted average common shares outstanding	13,890,882	13,813,048	13,874,661	13,789,603
Basic earnings (loss) per share	$ (0.01)	$ (0.01)	$ (0.03)	$ 0.03
Diluted earnings (loss) per share:				
Income (loss) applicable to common stock	$ (120,081)	$ (197,166)	$ (374,517)	$ 375,573
Weighted average common shares outstanding	13,890,882	13,813,048	13,874,661	13,789,603
Assuming conversion of options outstanding				291,836
Weighted average common shares outstanding, as adjusted	13,890,882	13,813,048	13,874,661	14,081,439
Diluted earnings (loss) per share	$ (0.01)	$ (0.01)	$ (0.03)	$ 0.03

For the three and six months ended June 30, 2008, options and restricted stock outstanding were not included in the computation of diluted earnings (loss) per share as the Company reported a loss from continuing operations available to common stockholders. For the three months ended June 30, 2007, options outstanding were not included in the computation of diluted earnings (loss) per share as the Company reported a loss from continuing operations available to common stockholders. For the six months ended June 30, 2007, options to purchase 101,063 shares of common stock at a weighted average price of $9.71 per share were outstanding, but were not included in the computation of diluted earnings per share as the options exercise price was greater than the average market price of the common shares. Options outstanding as of June 30, 2008 expire in December 2008.

5. Business Acquisitions

On October 12, 2007, the Company, through a wholly-owned subsidiary, Strong Digital Systems, Inc., acquired 100% of the outstanding shares of Marcel Desrochers, Inc. (MDI), a manufacturer and supplier of film and digital cinema screens, for cash consideration. As a result of the acquisition, MDI is forming a core business established to supply cinema screens to the digital and film cinema marketplace. The total purchase price of MDI at the date of acquisition was $2.5 million including cash acquired. The purchase price excluded an additional $0.9 million of restricted funds that were placed in escrow to secure certain indemnification and other obligation contingencies. Funds for the purchase were provided by internally generated cash flows. Direct transaction costs related to the acquisition amounted to $0.4 million.

Goodwill recorded in connection with these acquisitions represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired and are expected to be deductible for tax purposes.

Ballantyne of Omaha, Inc. and Subsidiaries
Notes to the Condensed Consolidated Financial Statements
Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

6. Comprehensive Income (Loss)

The accumulated other comprehensive income (loss), net, shown in the Company s consolidated balance sheets includes the unrealized loss on investments in securities, pension liability adjustments and the accumulated foreign currency translation adjustment. The following table shows the difference between the Company s reported net earnings and its comprehensive income:

	Three Months Ended June 30,		Six Months Ended June 30,	
$ in thousands	**2008**	**2007**	**2008**	**2007**
Comprehensive income (loss):				
Net income (loss)	$ (120,081)	$ (197,166)	$ (374,517)	$ 375,573
Other comprehensive income (loss):				
Unrealized gain (loss) on investment in securities	96,375		(946,345)	
Foreign currency translation adjustment	30,576		(128,690)	
Total comprehensive income (loss)	$ 6,870	$ (197,166)	$ (1,449,552)	$ 375,573

7. Sale of Product Line

During the second quarter, the Company sold its Coater and Marinade product line in exchange for $275,000 in cash. In connection with the sale, the Company recorded a pre-tax net gain of approximately $258,000 ($159,000 after-tax) which is net of related costs to sell. The product line was sold to a former Chief Financial Officer of the Company.

The Company recorded the sale of the Coater and Marinade product line in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. Based on the guidance, the Coater and Marinade product line is not considered a separate accounting component of the Company as the cash flows of the product line cannot be clearly distinguished from the rest of the Company. Therefore, Company has not presented the operations of the Coater and Marinade product line as discontinued operations.

8. Fair Value of Financial Instruments

Effective January 1, 2008, the Company adopted the provisions of SFAS No. 157, Fair Value Measurements (SFAS No. 157) which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements with respect to financial assets and liabilities. Under SFAS No. 157, fair value is the price to sell an asset or transfer a liability between market participants as of the measurement date. Fair value measurements assume the asset or liability is exchanged in an orderly manner; the exchange is in the principal market for that asset or liability (or in the most advantageous market when no principal market exists); and the market participants are independent, knowledgeable, able and willing to transact an exchange. Pursuant to the provisions of FSP No. 157-2, the Company has decided to defer adoption of SFAS No. 157 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis.

Ballantyne of Omaha, Inc. and Subsidiaries
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SFAS No. 157 establishes a hierarchy for fair value measurements based upon observable independent market inputs and unobservable market assumptions. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Considerable judgment is required in interpreting market data used to develop the estimates of fair value. The following represents the three categories of inputs used in determining the fair value of financial assets and liabilities:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are used in the measurement of assets and liabilities. Unobservable inputs require management to make certain projections and assumptions about the information that would be used by market participants in pricing the asset or liability.

Because of the inability to trade these investments, a readily determinable fair value using market observables (Level 1 input) does not exist. Therefore, in accordance with SFAS No. 157, Fair Value Measurement, the Company obtained Gifford Fong Associates, a third party valuation expert, to assist with the determination of the estimated fair value of its auction-rate securities (Level 3 input). The valuation expert used a cash flow model to determine the fair value of these securities. The significant inputs and assumptions used in preparing this model are summarized as follows:

- Interest rate indices LIBOR curve and commercial paper rates obtained.
- Rating transition matrix the rating transition matrix gives transition probabilities for the underlying collateral migrating from one rating level to another in one year, particularly the transition probability to default status. The rating transition matrix is constructed from rating migration and default data published by various rating agencies.
- Default and recovery rates the default rate is estimated using a credit spread (discount margin) over the risk free rate curve obtained.
- Illiquidity risk in a distressed market, investors may not be able to find willing buyers, hence reduced liquidity.
- Estimate for the timing of full redemption of the securities the full redemption is estimated to take place in two years on the historical observation that economic cycles usually turn around in two years.
- Estimated weighted average coupon the yield, considered to be the weighted average cost of capital (WACC), is related to the financial strength and outlook of each fund.

Financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2008 are summarized in the following table by the type of inputs applicable to the fair value measurements under the provisions of SFAS No. 157:

		Fair Value Measurements at Reporting Date Using		
Description	**6/30/08**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Available-for-sale securities	$ 10,828,655	$	$	$ 10,828,655
Total	$ 10,828,655	$	$	$ 10,828,655

A reconciliation of assets and liabilities measured at fair value on a recurring basis with the use of significant unobservable inputs (Level 3) from January 1, 2008 to June 30, 2008 follows:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)	
	Investments in Auction-Rate Securities	**Total**
Beginning balance	$ 13,000,000	$ 13,000,000
Total gains or losses (realized/unrealized)		
Included in income (or changes in net assets)		
Included in other comprehensive income (loss)	(946,345)	(946,345)
Purchases, issuances and settlements	(1,225,000)	(1,225,000)
Transfers in and/or out of Level 3		
Ending balance	$ 10,828,655	$ 10,828,655
The amount of total gains or losses for the period included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses relating to assets still held at the reporting date		

Ballantyne of Omaha, Inc. and Subsidiaries
Notes to the Condensed Consolidated Financial Statements
Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

9. Investments

The Company has certain investments in auction-rate securities which are classified as available-for-sale securities. Interest rates on these auction-rate securities are reset through an auction process that resets the applicable interest at pre-determined intervals every seven days. The investment securities are held within closed-end funds that continue to be AAA rated and fully collateralized at a minimum 200% net asset to fund ratio. The Company accounts for its investments in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities .

During 2008, the market for the Company s investments in auction-rate securities began experiencing a liquidity issue when the securities came up for auction due to an imbalance of buyers and sellers for the securities. The Company cannot predict how long the current imbalance in the auction market will continue. As a result, for a period of time, the Company may be unable to liquidate the auction rate securities held until a successful auction occurs or the securities are redeemed by the issuer of the investments. Based on the continued unsuccessful auctions of these investments, the investment securities have been reclassified to noncurrent assets within the Consolidated Balance Sheet as of June 30, 2008.

Due to the inability to trade all of the Company s investments in auction-rate securities in the current market, the Company continues to earn interest on its investments at the maximum contractual default rate. The weighted average maximum contractual default rate being earned is 3.22%.

Based on the valuations performed (Note 8), the Company determined there was an impairment in the fair value of its investments of approximately $0.9 million. When events or circumstances exist that require the Company to record an impairment on its investments, the Company determines whether the impairment should be classified as temporary or other-than-temporary. A temporary impairment charge results in an unrealized loss being recorded in the other comprehensive income (loss) component of stockholders equity. Such an unrealized loss does not affect net income (loss) for the applicable accounting period. An other-than-temporary impairment charge is recorded as a realized loss in the consolidated statement of operations and reduces net income (loss) for the applicable accounting period. The differentiating factors between temporary and other-than temporary impairment are primarily the length of the time and the extent to which the market value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in market value. Based on this assessment as of June 30, 2008, the Company determined the impairment in the fair value of its investments is temporary.

Ballantyne of Omaha, Inc. and Subsidiaries
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Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

10. Inventories

Inventories consist of the following:

	June 30, 2008	December 31, 2007
Raw materials and components	$ 6,194,052	$ 4,911,345
Work in process	1,271,300	772,055
Finished goods	4,116,411	4,200,155
	$ 11,581,763	$ 9,883,555

The inventory balances are net of reserves of approximately $2,430,000 and $1,901,000 as of June 30, 2008 and December 31, 2007, respectively.

11. Property, Plant and Equipment

Property, plant and equipment include the following:

	June 30, 2008	December 31, 2007
Land	$ 313,500	$ 313,500
Buildings and improvements	3,962,989	3,962,989
Machinery and equipment	7,442,365	7,199,257
Office furniture and fixtures	1,867,758	1,662,578
	13,586,612	13,138,324
Less accumulated depreciation	(9,922,231)	(9,505,200)
Net property, plant and equipment	$ 3,664,381	$ 3,633,124

Depreciation expense amounted to approximately $232,000 and $452,000 for the three and six months ended June 30, 2008, respectively, as compared to approximately $267,000 and $537,000 for the three and six months ended June 30, 2007.

12. Income Taxes

Income taxes are accounted for under the asset and liability method. The Company uses an estimate of its annual effective rate based on the facts and circumstances at the time while the actual effective rate is calculated at year-end. The Company recorded a receivable for the amount of the income tax refund due to the Company primarily as a result of estimated payments made by the Company during 2007 in excess of the amounts actually owed. The Company also has recorded a receivable for the carry back of certain net operating losses to previous year s taxable income resulting in an additional tax refund due. In addition, during the second quarter of 2008, the Company recorded an adjustment of approximately $50,000 to correct for a subsidiary s underaccrual of income taxes owed at December 31, 2007. Management determined that the effect of this item on previously reported periods was not material.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Company has adopted the provisions of FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a recognition threshold and measurement attribute for the financial statement recognition and

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measurement of a tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The adoption of this interpretation did not have a material impact on the Company s consolidated financial position.

The Company s uncertain tax positions are related to tax years that remain subject to examination by the relevant taxable authorities. The Company has examinations not yet initiated for Federal purposes for fiscal years 2004 through 2007. In most cases, the Company has examinations open for state or local jurisdictions based on the particular jurisdictions statute of limitations. The Company does not currently have any examinations in process.

An estimate for the underpayment of income taxes, including interest and penalties are classified as a component of tax expense in the consolidated statements of operations. The estimate approximated $0.2 million as of June 30, 2008 and December 31, 2007, respectively. The accruals largely related to state tax matters.

13. Warranty Reserves

The Company generally grants a warranty to its customers for a one-year period following the sale of all new equipment and on selected repaired equipment for a one-year period following the repair. The warranty period is extended under certain circumstances and for certain products. The Company accrues for these costs at the time of sale or repair, when events dictate that additional accruals are necessary. The following table summarizes warranty activity for the periods indicated below:

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Warranty accrual at beginning of period	$ 392,159	$ 578,703	$ 381,710	$ 617,052
Charged to expense	52,553	49,693	101,552	92,943
Amounts written off, net of recoveries	(97,141)	(112,195)	(135,691)	(193,794)
Warranty accrual at end of period	$ 347,571	$ 516,201	$ 347,571	$ 516,201

14. Debt

We are a party to a revolving credit facility (the Original Credit Facility) with First National Bank of Omaha expiring August 28, 2008. The Company intends to renew the credit facility prior to its expiration. The credit facility provides for borrowings up to the lesser of $4.0 million or amounts determined by an asset-based lending formula, as defined. Borrowings available under the credit facility amounted to $4.0 million at June 30, 2008. No amounts are currently outstanding. We pay interest on outstanding amounts equal to the Prime Rate plus 0.25% (5.25% at June 30, 2008) and pay a fee of 0.125% on the unused portion.

Effective March 31, 2008, the Company entered into a Seventh Amendment to its Original Credit Facility to allow an interim extension of credit (the Interim Credit Facility) in the amount of $10.4 million in addition to the $4.0 million allowed under the Original Credit Facility. The Interim Credit Facility is evidenced by a Promissory Note with an interest rate set at a floating rate set to after-tax interest income received on certain investment securities as defined in the Seventh Amendment. The Interim Credit Facility expires on March 30, 2009. The credit facilities contain certain restrictions primarily related to restrictions on acquisitions and dividends. All of the Company s personal property and certain stock in its subsidiaries secure the credit facilities. No amounts are currently outstanding under either of the credit facilities.

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15. Note Receivable

During July 2006, the Company entered into a note receivable arrangement with Digital Link LLC (Digital Link) pertaining to the sale and installation of digital projectors. The sale amounted to $780,000 of which 25% was due upon installation and was collected. The remaining amounts are due over a 5-year period at an 8% interest rate. At June 30, 2008, $386,883 is due from Digital Link. Only the payments received since inception in 2006 on the note receivable totaling $393,117 were recorded as revenue with the remaining amounts to be recognized as revenue in future periods when payment is received from Digital Link as described in the note receivable arrangement or when collections from the Digital Link can be reasonably assured. Additionally, until collections from Digital Link can be reasonably assured, no receivable will be recorded on this transaction. The costs incurred with the sale of projectors to Digital Link were expensed during 2006 with no future associated costs to be incurred.

16. Supplemental Cash Flow Information

Supplemental disclosures to the consolidated statements of cash flows are as follows:

	Six Months Ended June 30, 2008		2007	
Cash paid during the period for:				
Interest	$	3,514	$	8,770
Income taxes	$	470,434	$	912,920
Non-cash investing activities:				
Non-cash investment in joint venture	$		$	2,543,771

17. Stock Compensation

The Company accounts for awards of share-based compensation in accordance with Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment*, (SFAS No. 123(R)) which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors based on estimated fair values. Share-based compensation expense was $56,524 and $24,729 for the three months ended June 30, 2008 and 2007 and $75,022 and $54,067 for the six months ended June 30, 2008 and 2007, respectively.

Stock Options

The Company currently maintains a 2005 Outside Directors Stock Option Plan (2005 Outside Directors Plan) which has been approved by the Company s stockholders. During the current period, the Board of Directors made the decision to discontinue granting further stock options under this Plan. The Company also maintains a 1995 Employee Stock Option Plan and a 1995 Directors Stock Plan which both expired in 2005, however, there are outstanding stock options remaining under these two expired plans.

All past and future grants under the Company s stock option plans were granted at prices based on the fair market value of the Company s common stock on the date of grant. The outstanding options generally vest over periods ranging from zero to three years from the grant date and expire between 5 and 10 years after the grant date. No stock options were granted during the six months ended June 30, 2008 and 2007, respectively.

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The following table summarizes the Company s activities with respect to its stock options for the six months ended June 30, 2008:

	Number of Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Options outstanding at December 31, 2007	443,750	$ 2.33	3.41	$ 1,594,983
Granted				
Exercised	(73,625)	$ 0.80		
Forfeited				
Outstanding at June 30, 2008	370,125	$ 2.63	2.97	$ 787,675
Exercisable at June 30, 2008	370,125	$ 2.63	2.97	$ 787,675

The aggregate intrinsic value in the table above represents the total that would have been received by the option holders if all in-the-money options had been exercised on June 30, 2008.

The following table summarizes information about stock options outstanding and exercisable at June 30, 2008:

	Options outstanding at June 30, 2008			Exercisable at June 30, 2008		
Range of option exercise price	Number of options	Weighted average remaining contractual life	Weighted average exercise price per option	Number of options	Weighted average remaining contractual life	Weighted average exercise price per option
$ 0.62 to 0.63	210,000	3.83	$ 0.62	210,000	3.83	$ 0.62
$ 4.25 to 4.75	118,125	2.32	4.55	118,125	2.32	4.55
$ 7.30	42,000	0.51	7.30	42,000	0.51	7.30
$ 0.62 to 7.30	370,125	2.97	$ 2.63	370,125	2.97	$ 2.63

Restricted Stock Plan

During 2005, the Company adopted and the stockholders approved, the 2005 Restricted Stock Plan. Under terms of the plan, the compensation committee of the Board of Directors selects which employees of the Company are to receive restricted stock awards and the terms of such awards. The total number of shares reserved for issuance under the plan is 250,000 shares. The plan expires in September 2010. During May 2008, the Company granted 54,000 shares to certain employees. A portion of the shares vest at January 2009 with the remaining shares being earned if the Company achieves certain earning thresholds, as defined within the restricted stock agreements. Once the shares are earned, vesting would occur on January 1, 2010. At June 30, 2008, 196,000 shares remain available for issuance under the Plan.

On May 21, 2008, the Company s Stockholders approved the Ballantyne of Omaha, Inc. Non-Employee Director Restricted Stock Plan (Non-Employee Plan) to replace the 2005 Non-Employee Director Stock Option Plan. The total number of shares reserved for issuance under the plan is 120,000 shares. During May 2008, the Company granted 15,000 restricted shares under the Non-Employee Plan. The shares vest the day after the Company s 2009 Annual Meeting. At June 30, 2008, 105,000 shares remain available for issuance under the Plan.

In connection with restricted stock granted to certain employees and non-employee directors, the Company is accruing compensation expense based on the estimated number of shares expected to be issued utilizing the most current information available to the Company at the date of the financial statements.

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Employee Stock Purchase Plan

The Company s Employee Stock Purchase Plan, approved by the stockholders, provides for the purchase of shares of Ballantyne common stock by eligible employees at a per share purchase price equal to 85% of the fair market value of a share of Ballantyne common stock at either the beginning or end of the offering period, as defined, whichever is lower. Purchases are made through payroll deductions of up to 10% of each participating employee s salary. The maximum number of shares that can be purchased by participants in any offering period is 2,000 shares. Additionally, the Plan has set certain limits, as defined, in regard to the number of shares that may be purchased by all eligible employees during an offering period. At June 30, 2008, 123,746 shares of common stock remained available for issuance under the Plan. The Plan expires in October 2010.

18. Postretirement Health Care

Components of the net period benefit cost for the Company s post retirement health care plan includes:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Net periodic benefit cost:				
Service cost	$	$ 2,979	$	$ 5,958
Interest cost	4,974	5,420	9,948	10,838
Amortization of prior-service cost		5,597		11,195
Total net periodic benefit cost	$ 4,974	$ 13,996	$ 9,948	$ 27,991

The Company expects to pay $20,874 of benefits under its postretirement benefit plan in 2008. As of June 30, 2008, benefits of $3,221 have been paid.

19. Subsequent Event

On July 28, 2008, the Company provided guarantee to a note entered into by its joint venture, Digital Link II, LLC to finance digital projection equipment deployed in the normal course of business. The loan provides for borrowings of approximately $1.3 million and bears interest equal to 7% per annum. The Company s guarantee of the note is limited to its 44.4% ownership percentage, which amounts to approximately $0.6 million. RealD, who holds a membership interest of 55.6% in the joint venture, has provided a guarantee for the remainder of the note outstanding, which amounts to approximately $0.7 million. The guarantees will expire by the end of 2011. Under the terms of the guarantees, the Company and RealD would be required to fulfill the guarantees should the joint venture be in default of its loan or contract terms.

20. Concentrations

The Company s top ten customers accounted for approximately 48% of 2008 consolidated net revenues and were primarily from the theatre segment. Trade accounts receivable from these customers represented approximately 47% of net consolidated receivables at June 30, 2008. Sales to Regal Cinemas, Inc. represented over 10% of consolidated sales. Additionally, receivables from Vari International and Marcus Cinemas each represented over 10% of net consolidated receivables at June 30, 2008. While the Company believes its relationships with such customers are stable, most arrangements are made by purchase order and are terminable at will by either party. A significant decrease or interruption in business from its significant customers could have a material adverse effect on the Company s business, financial condition and results of operations. It could also be adversely affected by such factors as changes in foreign currency rates and weak economic and political conditions in each of the countries in which it sells its products.

Financial instruments that potentially expose the Company to a concentration of credit risk primarily consist of accounts receivables. The Company sells product to a large number of customers in many different geographic regions. To minimize credit concentration risk, the Company performs ongoing credit evaluations of its customers financial condition.

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21. Litigation

Ballantyne is currently a defendant in an asbestos case entitled *Larry C. Stehman and Leila Stehman v. Asbestos Corporation, Limited and Ballantyne of Omaha, Inc. individually and as successor in interest to Strong International, Strong Electric Corporation and Century Projector Corporation, et al*, filed December 8, 2006 in the Superior Court of the State of California, County of San Francisco. The Company believes that it has strong defenses and intends to defend the suit vigorously. It is not possible at this time to predict the outcome of this case, or the amount of damages, if any, that a jury may award. The plaintiffs have made no monetary demand upon Ballantyne. It is possible that an adverse resolution of this case could have a material adverse effect on the Company s financial position.

22. Business Segment Information

The presentation of segment information reflects the manner in which management organizes segments for making operating decisions and assessing performance.

As of June 30, 2008, the Company s operations were conducted principally through two business segments: Theatre and Lighting. Theatre operations include the design, manufacture, assembly, sale and service of motion picture projectors, motion picture screens, xenon lamphouses and power supplies, sound systems, film handling equipment and the sale and service of xenon lamps, lenses and digital projection equipment. The lighting segment operations include the design, manufacture, assembly and sale of follow spotlights, stationary searchlights and computer operated lighting systems for the motion picture production, television, live entertainment, theme parks and architectural industries. The Company allocates resources to business segments and evaluates the performance of these segments based upon reported segment gross profit. However, certain key operations of a particular segment are tracked on the basis of operating profit. All intersegment sales are eliminated in consolidation.

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Summary by Business Segments

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Net revenue				
Theatre				
Products	$ 11,610,471	$ 10,571,798	$ 23,823,408	$ 21,363,959
Services	753,853	922,323	1,520,614	1,857,703
Total theatre	12,364,324	11,494,121	25,344,022	23,221,662
Lighting	1,235,735	973,505	2,310,952	2,017,873
Other	43,045	192,368	185,302	351,209
Total revenue	$ 13,643,104	$ 12,659,994	$ 27,840,276	$ 25,590,744
Gross profit				
Theatre				
Products	$ 2,326,435	$ 2,225,839	$ 4,541,535	$ 4,404,380
Services	(599,177)	4,044	(864,791)	221,927
Total theatre	1,727,258	2,229,883	3,676,744	4,626,307
Lighting	302,599	170,148	602,172	423,724
Other	19,998	82,182	80,820	153,966
Total gross profit	2,049,855	2,482,213	4,359,736	5,203,997
Selling and administrative expenses:				
Selling	(742,718)	(709,736)	(1,530,520)	(1,492,352)
Administrative	(1,634,972)	(1,594,003)	(3,660,268)	(3,027,050)
Goodwill impairment		(639,466)		(639,466)
Gain on transfer of assets		1,230		234,557
Gain on sale of assets	258,170		258,170	
Loss on disposal of fixed assets			(1,285)	(11,004)
Operating income (loss)	(69,665)	(459,762)	(574,167)	268,682
Net interest income	120,187	198,033	257,838	406,089
Equity in loss of joint venture	(184,909)	(73,380)	(297,900)	(73,380)
Other income (expense), net	19,882	(24,731)	46,674	(72,752)
Income (loss) before income taxes	$ (114,505)	$ (359,840)	$ (567,555)	$ 528,639
Expenditures on capital equipment				
Theatre				
Products	$ 141,462	$ 52,114	$ 316,636	$ 124,338
Services	46,778	41,373	161,097	73,105
Total theatre	188,240	93,487	477,733	197,443
Lighting	4,695	3,726	14,382	9,335
Total	$ 192,935	$ 97,213	$ 492,115	$ 206,778
Depreciation and amortization				
Theatre				
Products	$ 555,667	$ 508,379	$ 1,110,838	$ 994,474
Services	62,860	49,951	120,478	95,101
Total theatre	618,527	558,330	1,231,316	1,089,575
Lighting	17,299	22,040	34,285	35,840
Total	$ 635,826	$ 580,370	$ 1,265,601	$ 1,125,415

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Summary by Business Segments (continued)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Loss on disposal of fixed assets				
Theatre				
Products	$	$	$ (1,285)	$ (11,004)
Services				
Total theatre			(1,285)	(11,004)
Lighting				
Total	$	$	$ (1,285)	$ (11,004)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Gain on transfer of assets				
Theatre				
Products	$	$ 1,230	$	$ 234,557
Services				
Total theatre		1,230		234,557
Lighting				
Total	$	$ 1,230	$	$ 234,557

	June 30, 2008	December 31, 2007
Identifiable assets		
Theatre		
Products	$ 46,150,466	$ 47,442,283
Services	1,991,549	2,195,660
Total theatre	48,142,015	49,637,943
Lighting	3,994,912	3,970,457
Other	297,871	531,948
Total identifiable assets	$ 52,434,798	$ 54,140,348

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Summary by Business Segments (continued)

Summary by Geographical Area

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Net revenue				
United States	$ 8,714,578	$ 9,794,217	$ 18,885,559	$ 20,248,461
Canada	291,117	170,924	784,670	246,304
Asia	2,135,629	1,554,170	3,913,414	2,892,275
Latin America	1,566,422	679,164	2,821,733	1,317,477
Europe	615,166	260,119	1,017,820	683,950
Other	320,192	201,400	417,080	202,277
Total	$ 13,643,104	$ 12,659,994	$ 27,840,276	