UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 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 September 30, 2012

OR

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

For the transition period from to

NORTECH SYSTEMS INCORPORATED

Commission file number **0-13257**

State of Incorporation: **Minnesota**

IRS Employer Identification No. **41-1681094**

Executive Offices: **1120 Wayzata Blvd E., Suite 201, Wayzata, MN 55391**

Telephone number: **(952) 345-2244**

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

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 Regulations 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 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 the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer o	Accelerated Filer o
Non-accelerated Filer o	Smaller Reporting Company x

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

Number of shares of $.01 par value common stock outstanding at November 1, 2012 - 2,742,992

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PART 1

ITEM 1. FINANCIAL STATEMENTS

NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

	SEPTEMBER 30 2012 (Unaudited)	DECEMBER 31 2011
ASSETS		
Current Assets		
Cash	$	$
Accounts Receivable, Less Allowance for Uncollectible Accounts	15,493,550	16,720,462
Inventories	17,686,322	19,029,593
Prepaid Expenses	811,677	572,140
Income Taxes Receivable	46,024	170,292
Deferred Income Taxes	855,000	805,000
Total Current Assets	34,892,573	37,297,487
Property and Equipment, Net	9,143,005	9,083,874
Finite Life Intangible Assets, Net of Accumulated Amortization	46,301	61,547
Other Assets	339,235	339,235
Total Assets	$ 44,421,114	$ 46,782,143

	SEPTEMBER 30 2012	DECEMBER 31 2011
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities		
Line of Credit	$ 7,875,648	$ 9,345,044
Current Maturities of Long-Term Debt	438,349	1,310,210
Accounts Payable	8,427,581	11,333,013
Accrued Payroll and Commissions	2,596,216	2,170,852
Other Accrued Liabilities	979,406	852,936
Total Current Liabilities	20,317,200	25,012,055
Long-Term Liabilities		
Long-Term Debt, Net of Current Maturities	2,860,242	812,917
Deferred Income Taxes	241,000	271,000
Other Long-Term Liabilities	142,983	180,378
Total Long-Term Liabilities	3,244,225	1,264,295
Total Liabilities	23,561,425	26,276,350
Shareholders Equity		
Preferred Stock, $1 par value; 1,000,000 Shares Authorized: 250,000 Shares Issued and Outstanding	250,000	250,000
	27,430	27,430

Common Stock - $0.01 par value; 9,000,000 Shares Authorized: 2,742,992 Shares Issued and Outstanding				
Additional Paid-In Capital		15,725,392		15,725,392
Accumulated Other Comprehensive Loss		(62,936)		(62,936)
Retained Earnings		4,919,803		4,565,907
Total Shareholders Equity		20,859,689		20,505,793
Total Liabilities and Shareholders Equity	$	44,421,114	$	46,782,143

See Accompanying Condensed Notes to Consolidated Financial Statements

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NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30 2012	2011
Net Sales	$ 25,520,963	$ 28,318,158
Cost of Goods Sold	22,736,923	25,029,395
Gross Profit	2,784,040	3,288,763
Operating Expenses:		
Selling Expenses	992,295	900,849
General and Administrative Expenses	1,463,074	1,967,776
Total Operating Expenses	2,455,369	2,868,625
Income From Operations	328,671	420,138
Other Expense		
Interest Expense	(111,999)	(130,152)
Miscellaneous Expense, net	(54,507)	(9,121)
Total Other Expense	(166,506)	(139,273)
Income Before Income Taxes	162,165	280,865
Income Tax Expense	57,000	98,000
Net Income	$ 105,165	$ 182,865
Earnings Per Common Share:		
Basic and Diluted	$ 0.04	$ 0.07
Weighted Average Number of Common Shares Outstanding Used for Basic and Diluted Earnings Per Common Share	2,742,992	2,742,992

See Accompanying Condensed Notes to Consolidated Financial Statements

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NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30			
		2012		**2011**
Net Sales	$	81,915,222	$	85,112,931
Cost of Goods Sold		73,031,193		75,392,663
Gross Profit		8,884,029		9,720,268
Operating Expenses:				
Selling Expenses		3,232,919		2,701,642
General and Administrative Expenses		4,675,422		5,972,692
Total Operating Expenses		7,908,341		8,674,334
Income From Operations		975,688		1,045,934
Other Income (Expense)				
Interest Expense		(349,062)		(392,237)
Bargain Purchase Gain				791,615
Miscellaneous Expense, net		(80,730)		(55,165)
Total Other Income (Expense)		(429,792)		344,213
Income Before Income Taxes		545,896		1,390,147
Income Tax Expense		192,000		435,000
Net Income	$	353,896	$	955,147
Earnings Per Common Share:				
Basic and Diluted	$	0.13	$	0.35
Weighted Average Number of Common Shares Outstanding Used for Basic and Diluted Earnings Per Common Share		2,742,992		2,742,992

See Accompanying Condensed Notes to Consolidated Financial Statements

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NORTECH SYSTEMS INCORPORATED AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30 2012	2011
Cash Flows From Operating Activities		
Net Income	$ 353,896	$ 955,147
Adjustments to Reconcile Net Income to Net Cash Provided by (Used in) Operating Activities:		
Depreciation	1,382,757	1,446,212
Amortization	15,246	105,452
Stock-Based Compensation		23,792
Interest on Swap Valuation		(18,140)
Bargain Purchase Gain		(791,615)
Deferred Income Taxes	(80,000)	185,000
Loss on Disposal of Property and Equipment	3,490	941
Changes in Current Operating Items, Net of Effects of Business Acquisitions		
Accounts Receivable	1,226,912	(198,970)
Inventories	1,343,271	(5,287,685)
Prepaid Expenses and Other Assets	(239,537)	(165,016)
Income Taxes Receivable / Payable	124,268	224,941
Accounts Payable	(2,905,432)	1,220,948
Accrued Payroll and Commissions	425,364	142,454
Other Accrued Liabilities	83,709	(50,470)
Net Cash Provided by (Used in) Operating Activities	1,733,944	(2,207,009)
Cash Flows from Investing Activities:		
Proceeds from Sale of Property and Equipment	36,856	1,400
Business Acquisitions		(1,042,389)
Purchase of Property and Equipment	(1,476,868)	(560,022)
Net Cash Used in Investing Activities	(1,440,012)	(1,601,011)
Cash Flows from Financing Activities:		
Net Borrowings (Repayments) on Line of Credit	(1,469,396)	3,648,695
Proceeds from Long-Term Debt	1,600,970	1,380,904
Principal Payments on Long-Term Debt	(425,506)	(1,452,161)
Net Cash Provided by (Used in) Financing Activities	(293,932)	3,577,438
Net Decrease in Cash		(230,582)
Cash - Beginning		230,582
Cash - Ending	$	$
Supplemental Disclosure of Cash Flow Information:		
Cash Paid During the Period for Interest	$ 293,740	386,612
Cash Paid During the Period for Income Taxes	116,155	
Supplemental Noncash Investing and Financing Activities		
Due to Seller for Business Acquisition	$	250,000
Capital Expenditures in Accounts Payable		117,324

See Accompanying Condensed Notes to Consolidated Financial Statements

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CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited consolidated financial statements for the interim periods have been prepared in accordance with Generally Accepted Accounting Principles in the United States of America (GAAP) for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the financial information and footnotes required by GAAP for complete financial statements, although we believe the disclosures are adequate to make the information presented not misleading. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in our latest shareholders annual report on Form 10-K. The operating results for the interim periods presented are not necessarily indicative of the results expected for the full year or for any other interim period. In our opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. In preparing these consolidated financial statements, we have made our best estimates and judgments of certain amounts included in the consolidated financial statements, giving due consideration to materiality. Changes in the estimates and assumptions used by us could have a significant impact on our financial results, since actual results could differ from those estimates.

Principles of Consolidation

The consolidated financial statements include the accounts of Nortech Systems Incorporated and its wholly owned subsidiary, Manufacturing Assembly Solutions of Monterrey, Inc. All significant intercompany accounts and transactions have been eliminated.

Revenue Recognition

We recognize revenue upon shipment of manufactured products to customers, when title has passed, all contractual obligations have been satisfied and collection of the resulting receivable is reasonably assured. We also provide engineering services separate from the manufacture of a product. Revenue for engineering services is recognized upon completion of the engineering process, providing standalone fair value to our customers. Our engineering services are short-term in nature. In addition, we have another separate source of revenue that comes from short-term repair services, which are recognized upon completion of the repairs and shipment of product back to the customer. Shipping and handling costs charged to our customers are included in net sales, while the corresponding shipping expenses are included in cost of goods sold.

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Stock Options

Following is the status of all stock options as of September 30, 2012, including changes during the nine-month period then ended:

	Shares	Weighted-Average Exercise Price Per Share		Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding - January 1, 2012	623,600	$	7.33		
Forfeited	(11,250)	$	7.83		
Cancelled	(319,600)	$	7.43		
Outstanding - September 30, 2012	292,750	$	7.19	2.72	$
Exercisable - September 30, 2012	292,750	$	7.19	2.72	$

There were no options exercised during the three and nine months ended September 30, 2012 and 2011.

Total compensation expense related to stock options for the three months ended September 30, 2012 and 2011 was $0 and $7,930, respectively. Total compensation expense related to stock options for the nine months ended September 30, 2012 and 2011 was $0 and $23,792, respectively. As of September 30, 2012, there was no unrecognized compensation expense as all options were fully vested.

In January 2012, the Board of Directors terminated the 2007 FOCUS Incentive plan and as a result all 319,600 outstanding stock options under this plan were cancelled.

Equity Appreciation Rights Plan

In November 2010, the Board of Directors approved the adoption of the Nortech Systems Incorporated Equity Appreciation Rights Plan (the 2010 Plan). The total number of Equity Appreciation Right Units (Units) the Plan can issue shall not exceed an aggregate of 750,000 Units, of which 100,000 Units were granted during the year ended December 31, 2010 with a redemption date of December 31, 2012. On March 7, 2012, we granted an additional 250,000 Units with redemption dates ranging from December 31, 2014 through December 31, 2016.

The 2010 Plan provides that Units granted shall fully vest three years from the designated base date unless terminated earlier. Units give the holder a right to receive a cash payment equal to the appreciation in book value per share of common stock from the base date, as defined, to the redemption date. Unit redemption payments under this plan shall be paid in cash within 90 days after we determine the book value of the Units as of the calendar year immediately preceding the redemption date.

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Total compensation expense related to these Units based on the estimated appreciation over their remaining terms was $4,690 and $10,193 for the three months ended September 30, 2012 and 2011, respectively, and $18,695 and $42,655 for the nine months ended September 30, 2012 and 2011, respectively. At September 30, 2012 and December 31, 2011, approximately $81,000 and $62,000 have been accrued under this plan. As of September 30, 2012, approximately $74,000 of this balance is included in Other Accrued Liabilities as it is an estimate of the amount to be paid within 12 months. The remaining $7,000 balance at September 30, 2012 and all of the balance at December 31, 2011 are included in Other Long-Term Liabilities.

Earnings per Common Share

For the three and nine months ended September 30, 2012 and 2011, the effect of all stock options is antidilutive. Therefore, no outstanding options were included in the computation of per-share amounts.

Segment Reporting Information

All of our operations fall under the Contract Manufacturing segment within the Electronic Manufacturing Services industry. We strategically direct production between our various manufacturing facilities based on a number of considerations to best meet our customers requirements. We share resources for sales, marketing, engineering, supply chain management, cash and risk management, banking, credit and collections, human resources, payroll, internal control, audit, taxes, SEC reporting and corporate accounting. Consolidated financial information is available that is evaluated regularly by the chief operating decision maker in assessing performance and allocating resources.

Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market (based on the lower of replacement cost or net realizable value). Costs include material, labor, and overhead required in the warehousing and production of our products. Inventory reserves are maintained for the estimated value of the inventories that may have a lower value than stated or quantities in excess of future production needs.

Inventories are as follows:

	September 30 2012	December 31 2011
Raw Materials	$ 13,713,514	$ 13,056,955
Work in Process	3,006,721	3,202,002
Finished Goods	2,447,632	3,880,764
Reserve	(1,481,545)	(1,110,128)
Total	$ 17,686,322	$ 19,029,593

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Finite Life Intangible Assets

Finite life intangible assets at September 30, 2012 and December 31, 2011 are as follows:

	September 30, 2012			
	Remaining Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Bond Issue Costs	9	$ 79,373	$ 33,072	$ 46,301
Customer Base	0	676,557	676,557	
Totals		$ 755,930	$ 709,629	$ 46,301

	December 31, 2011			
	Remaining Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Bond Issue Costs	10	$ 79,373	$ 29,106	$ 50,267
Customer Base	1	676,557	665,277	11,280
Totals		$ 755,930	$ 694,383	$ 61,547

Amortization expense for the three months ended September 30, 2012 and 2011 was $1,363 and $35,150, respectively. Amortization expense for the nine months ended September 30, 2012 and 2011 was $15,246 and $105,452, respectively. Estimated future amortization expense related to these assets is as follows:

Remainder of 2012	$ 1,000
2013	5,000
2014	5,000
2015	5,000
2016	5,000
Thereafter	25,000
Total	$ 46,000

NOTE 2. CONCENTRATION OF CREDIT RISK AND MAJOR CUSTOMERS

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash and accounts receivable. With regard to cash, we maintain our excess cash balances in checking accounts at one high-credit quality financial institution. These accounts may at times exceed federally insured limits. We grant credit to customers in the normal course of business and do not require collateral on our accounts receivable.

One customer accounted for 10% or more of our net sales for the three and nine months ended September 30, 2012 and 2011:

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	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
GE Medical Division	16%	18%	17%	16%
GE Transportation Division	7	9	7	8
Total GE Medical & Transportation Division	23%	27%	24%	24%

Accounts receivable from G.E. s Medical and Transportation Divisions represented 17% of total accounts receivable at September 30, 2012 and December 31, 2011.

Export sales represented 6% of consolidated net sales for the three and nine months ended September 30, 2012 and 2011.

NOTE 3. FINANCING ARRANGEMENTS

On May 2, 2012 we entered into the fourth amendment to the third amended and restated credit agreement with Wells Fargo Bank (WFB). The credit agreement with WFB provides for a line of credit arrangement of $13.5 million, which expires if not renewed, on May 31, 2015. The credit arrangement also has a $1.8 million real estate term note with a maturity date of March 31, 2027 which replaces the $0.9 million real estate term note that was to expire on May 31, 2012, and a new term loan of up to $2.0 million for capital expenditures to be made prior to December 31, 2013 with a maturity date of May 31, 2015. At September 30, 2012 we ve used $0.7 million of the $2.0 million

Both the line of credit and real estate term note are subject to variations in LIBOR rates. The weighted-average interest rate on our line of credit was 3.8% for the three and nine months ended September 30, 2012, while the weighted-average rate on our real estate term loan was 4.1% and 4.0% for the same periods, respectively. The line of credit, real estate term note, and equipment term loans with WFB contain certain covenants which, among other things, require us to adhere to regular reporting requirements, abide by annual shareholder dividend limitations, maintain certain financial performance, and limit the amount of annual capital expenditures. On September 30, 2012, we had outstanding advances of $7.9 million under the line of credit, with unused availability of $4.5 million supported by our borrowing base and we were in compliance with all covenants.

NOTE 4. INCOME TAXES

On a quarterly basis, we estimate what our effective tax rate will be for the full fiscal year and record a quarterly income tax provision based on the anticipated rate. As the year progresses, we refine our estimate based on the facts and circumstances by each tax jurisdiction. Our effective tax rate for the three months ended September 30, 2012 and 2011 was 35%. The effective tax rate for the year ended December 31, 2012 is expected to be 36% compared to 32% for the year

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ended December 31, 2011. The increase is principally due to the fact that the federal government has not yet extended the research and development credit for the 2012 tax year.

The differences between federal income taxes computed at the federal statutory rate and reported income taxes for the three and nine months ended September 30, 2012 and 2011 are as follows:

	Three Months Ended September 30		**Nine Months Ended September 30**
	2012	**2011**	**2012**