

ELECTRO SENSORS INC  
Form DEF 14A  
March 25, 2005

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

**SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of  
the Securities Exchange Act of 1934 (Amendment No. )

Filed by the Registrant ☒

Filed by a Party other than the Registrant ☐

Check the appropriate box:

- ☐ Preliminary Proxy Statement  
☐ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**  
☒ Definitive Proxy Statement  
☐ Definitive Additional Materials  
☐ Soliciting Material Pursuant to §240.14a-12

Electro-Sensors, Inc.  
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- ☒ No fee required.  
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**ELECTRO-SENSORS, INC. 6111 Blue Circle Drive Minnetonka, Minnesota 55343**

(952) 930-0100

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS  
To Be Held April 20, 2005**

To the Shareholders of Electro-Sensors Inc.:

Notice is hereby given that the Annual Meeting of Shareholders of Electro-Sensors, Inc. will be held at the Sheraton Bloomington, 7800 Normandale Boulevard, Bloomington, Minnesota, on Wednesday, April 20, 2005, at 2:00 pm, Central Standard Time, for the following purposes:

1. To set the number of directors at five (5);
2. To elect five (5) directors to serve until the next annual meeting of shareholders;
3. To ratify the selection of Virchow, Krause & Company, LLC as independent auditors for the Company for the fiscal year ending December 31, 2005; and
4. To take action upon any other business as may properly come before the meeting or any adjournment or postponement thereof.

Accompanying this Notice of Annual Meeting is a Proxy Statement, Form of Proxy and the Company's 10-KSB for the fiscal year ended December 31, 2004.

The Board of Directors has fixed the close of business on February 21, 2005 as the record date for the determination of shareholders entitled to notice of and to vote at the Annual Meeting of Shareholders.

BY ORDER OF THE BOARD OF DIRECTORS,

/s/ Bradley D. Slye

Bradley D. Slye  
President

Minnetonka, Minnesota

Dated: March 25, 2005

TO ASSURE YOUR REPRESENTATION AT THE MEETING, PLEASE SIGN, DATE AND RETURN YOUR PROXY IN THE ENCLOSED ENVELOPE, WHETHER OR NOT YOU EXPECT TO ATTEND IN PERSON. SHAREHOLDERS WHO ATTEND THE MEETING MAY REVOKE THEIR PROXIES AND VOTE IN PERSON IF THEY SO DESIRE.

**ELECTRO-SENSORS, INC. 6111 Blue Circle Drive Minnetonka, Minnesota 55343 (952) 930-0100**

**PROXY STATEMENT**

**FOR**

**ANNUAL MEETING OF SHAREHOLDERS**



To Be Held April 20, 2005

**GENERAL INFORMATION**



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This Proxy Statement is furnished by the Board of Directors (the "Board of Directors") of Electro-Sensors, Inc., a Minnesota corporation (the "Company"), to the shareholders of the Company in connection with a solicitation of proxies to be voted at the Annual Meeting of Shareholders (the "Annual Meeting") to be held at 2:00 p.m., Central Standard Time, on Wednesday, April 20, 2005, at the Sheraton Bloomington, 7800 Normandale Boulevard, Bloomington, Minnesota, and at any and all adjournments or postponements thereof. This Proxy Statement and the accompanying materials are first being mailed to shareholders on or about March 25, 2005.

If your shares are registered in the name of a bank or brokerage firm, you may be eligible to vote your shares electronically via the Internet or telephone. A large number of banks and brokerage firms are participating in the ADP Investor Communication Services online program. This program provides eligible shareholders who receive a paper copy of the Annual Report and Proxy Statement the opportunity to vote via the Internet or telephone. If your bank or brokerage firm is participating in ADP's program, your voting form will provide instructions. If your voting form does not refer to Internet or telephone information, please complete and return the paper proxy card in the postage paid envelope provided.

Any proxy delivered pursuant to this solicitation is revocable at the option of the person giving the proxy at any time before it is exercised. A proxy may be revoked, prior to its exercise, by executing and delivering a later-dated proxy via the Internet, via telephone or by mail, by delivering written notice of the revocation of the proxy to the Company's Secretary prior to the Annual Meeting, or by attending and voting at the Annual Meeting. Attendance at the Annual Meeting, in and of itself, will not constitute a revocation of a proxy. The shares represented by a proxy will be voted in accordance with the shareholder's directions if the proxy is duly submitted and not validly revoked prior to the Annual Meeting. If no directions are specified on a duly submitted proxy, the shares will be voted, in accordance with the recommendations of the Board of Directors, FOR approval of the number of directors to be set at five, FOR the election of the directors nominated by the Board of Directors, FOR the approval of auditors for the fiscal year ending December 31, 2005, and in accordance with the discretion of the persons appointed as proxies on any other matters properly brought before the Annual Meeting and any all adjournments or postponements thereof.

The expense of preparing, printing, and mailing this Proxy Statement and the proxies solicited hereby will be borne by the Company. The Company will request brokerage firms, banks, nominees, custodians, and fiduciaries to forward proxy materials to the beneficial owners of shares of Common Stock as of the record date, and will provide reimbursement for the cost of forwarding the proxy materials in accordance with customary practice. In addition to the use of the Internet and mail, proxies may be solicited by officers, directors, and regular employees of the Company, without additional remuneration, in person or by telephone, telegraph, or facsimile transmission.

## **OUTSTANDING SHARES & VOTING RIGHTS**

The Company fixed the close of business on February 21, 2005 as the record date for determining shareholders entitled to notice of and to vote at the Annual Meeting. At February 21, 2005, the Company had outstanding 3,219,212 shares of Common Stock, the only outstanding class of capital stock of the Company. Each share of Common Stock outstanding on the record date entitles the holder thereof to one (1) vote on each matter to be voted upon by shareholders at the Annual Meeting. Holders of Common Stock are not entitled to cumulative voting rights.

A majority of the shares of Common Stock entitled to vote at the Annual Meeting, present in person or by proxy, constitutes a quorum for the transaction of business. Abstentions are counted as shares present for purposes of determining the presence or absence of a quorum. Proxies relating to street name shares that are voted by brokers on some matters, but not on other matters as to which authority to vote is withheld from the broker ( broker non-votes ) absent voting instructions from the beneficial owner, will be treated as shares present for purposes of determining the presence or absence of a quorum. The Inspector of Election appointed by the Board of Directors will determine the shares represented at the meeting and the validity of proxies and ballots, and will count all votes and ballots.

## **CORPORATE GOVERNANCE**

The business affairs of the Company are conducted under the direction of the Board of Directors in accordance with the Minnesota Business Corporation Act and our Articles of Incorporation and Bylaws. Members of the Board of Directors are informed of our business through discussions with management, by reviewing materials provided to them and by participating in meetings of the Board of Directors and its committees, among other activities. The corporate governance practices that we follow are summarized below.

### **Independence**

The Board of Directors has determined that Messrs. Marino, Miller and Strom, constituting a majority the Board of Directors, are independent directors as defined by the listing standards of the Nasdaq Stock Market, since none of them are believed to have any relationships that, in the opinion of the Board of Directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. Mr. Slye is precluded from being considered independent by Nasdaq rules since he currently serves as an executive officer of the Company. Mr. Peterson is precluded from being considered independent by Nasdaq rules since he currently is employed by the Company.

The Board of Directors has determined that each member of the Company's Audit Committee, Compensation Committee and Nominating Committee are independent in accordance with the listing standards of the Nasdaq Stock Market.

### **Code of Ethics and Business Conduct**

The Company has adopted the Electro-Sensors Code of Ethics and Business Conduct (the Code of Conduct ), a code of conduct that applies to all of our directors, officers and employees. A copy of the Code of Conduct was provided with the Proxy Statement for the 2004 Annual Meeting

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of Shareholders and is also available upon written request to the Chief Executive Officer. If we make any substantive amendments to the Code of Conduct or grant any waiver, including any implicit waiver from a provision of the Code of Conduct to our directors or executive officers, we will disclose the nature of such amendments or waiver in a report on Form 8-K.

### **Director Attendance at Annual Meeting**

Directors' attendance at Annual Meetings can provide our shareholders with an opportunity to communicate with directors about issues affecting the Company, thus, all directors are expected to attend the Annual Meetings of Shareholders. Five directors attended the 2004 Annual Meeting of Shareholders.

### **Communications with the Board**

Shareholders may communicate directly with the Board of Directors. All communications should be directed to our Corporate Secretary at the address below and should prominently indicate on the outside of the envelope that it is intended for the Board of Directors or for non-management directors. If no director is specified, the communication will be forwarded to the entire Board. Shareholder communications to the Board should be sent to:

Board of Directors

Attention: Corporate Secretary

Electro-Sensors, Inc.

6111 Blue Circle Drive

Minnetonka, Minnesota 55343-9108

**Committees and Meetings of the Board of Directors**

The present standing committees of the Board of Directors are described below.

### **Board Meetings**

The Board of Directors met four times during the last fiscal year. No incumbent member of the Board of Directors attended fewer than 75% of the total number of meetings held by the Board of Directors and the committees on which he served (during the periods that he served).

### **Audit Committee**

Messrs. Strom, Marino, and Miller currently serve as members of the Audit Committee. This committee met twice during the last fiscal year. The Audit Committee is responsible for selecting the Company's independent auditors, and for assisting the Board of Directors in its oversight of corporate accounting and internal controls, reporting practices of the Company and the quality and integrity of the financial reports of the Company. The Audit Committee Charter specifies the composition and responsibilities of the committee. For more information concerning the Audit Committee, see the Report of the Audit Committee on page 11 and the Audit Committee Charter attached as Appendix A to the Proxy Statement for the 2004 Annual Meeting of Shareholders. The Board has named Geoff Miller as the audit committee financial expert as defined by Item 401(e) of Regulation S-B under the Securities Act of 1933. The Company acknowledges that the designation of Mr. Miller as the audit committee financial expert does not impose on Mr. Miller any duties, obligations or liability that are greater than the duties, obligations and liability imposed on Mr. Miller as a member of the Audit Committee and the Board of Directors in the absence of such designation or identification.

### **Compensation Committee**

Messrs. Strom, Marino and Miller currently serve as members of the Compensation/Stock Option Committee (the "Compensation Committee"). This committee met twice during the last fiscal year. The Compensation Committee is responsible for making recommendations to the Board of Directors concerning compensation of the Company's employees, officers, and directors, and is authorized to determine the compensation of the Company's executive officers. The Compensation Committee is authorized to administer the various incentive plans of the Company and has all powers of the attendant thereto, including the power to grant employee stock options.

### **Directors' Compensation**





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Directors who are not employees of the Company receive \$1,500 per each board and committee meeting for their services on the Board.

### **Nominating Committee**

Messrs. Strom, Marino, and Miller currently serve as members of the Nominating Committee. The Nominating Committee did not meet in fiscal year 2004. The Nominating Committee is responsible for evaluating and nominating or recommending candidates for the Company's Board of Directors. A copy of the Nominating Committee Charter, which has been adopted by the Company's Board of Directors, was attached as Appendix B to the Proxy Statement for the 2004 Annual Meeting of Shareholders.

*Nominating Policy*

The Nominating Committee will consider candidates for nomination as a director recommended by shareholders, directors, third party search firms and other sources. The Nominating Committee believes that candidates for directors should have certain minimum qualifications, including being able to read and understand basic financial statements, being over 18 years of age, having familiarity with the Company's business and industry, having high moral character and mature judgment, being able to work collegially with others, and not currently serving on more than three Boards of public companies. The Nominating Committee may modify these minimum qualifications from time to time.

In evaluating director nominees who meet the Company's minimum qualifications, the Nominating Committee considers the following factors and qualifications, among others:

the appropriate size and the diversity of the Company's Board of Directors;

the needs of the Board with respect to the particular talents and experience of its directors;

the knowledge, skills and experience of nominees, including experience in technology, business, finance, administration or public service, in light of prevailing business conditions and the knowledge, skills and experience already possessed by other members of the Board;

familiarity with domestic and international business matters;

age and legal and regulatory requirements;

experience with accounting rules and practices;

appreciation of the relationship of the Company's business to the changing needs of society; and

the desire to balance the considerable benefit of continuity with the periodic injection of the fresh perspective provided by new members.

The Nominating Committee will consider the attributes of the candidates and the needs of the board, and will review all candidates in the same manner.

A shareholder who wishes to recommend one or more directors must provide a written recommendation to the Secretary of the Company at the address below at least 120 days prior to the mailing of the proxy statement for the next Annual Meeting of Shareholders. Notice of a recommendation must include name and address of the shareholder and the class and number of shares such shareholder owns. With respect to the nominee, the shareholder should include the nominee's name, age, business address, residence address, current principal occupation, five year employment history with employer names and a description of the employer's business, the number of shares beneficially owned by the nominee, whether such nominee can read and understand basic financial statements, and other board memberships, if any.

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Electro-Sensors, Inc.

Attn: Corporate Secretary

6111 Blue Circle Drive

Minnetonka, MN 55343-9108

The recommendation must be accompanied by a written consent of the nominee to stand for election at the Annual Meeting if nominated by the Nominating Committee and to serve if elected by the shareholders. The Company may require any nominee to furnish additional information that may be needed to determine the eligibility of the nominee and whether the nominee has the attributes the Board believes are important in its composition.

**ELECTION OF DIRECTORS****Proposals #1 and #2**

The Bylaws of the Company provide that the shareholders at each annual meeting shall determine the number of directors, which shall not be less than one. The Nominating Committee and the Board of Directors recommends that the number of directors be set at five and that five directors be elected at the Annual Meeting to serve until the next Annual Meeting or until their successors are duly elected and qualified. Under applicable Minnesota law, approval of the proposal to set the number of directors at five requires the affirmative vote of the holders of the greater of (1) a majority of the voting power of the shares represented in person or by proxy at the annual meeting with authority to vote on such matter or (2) a majority of the voting power of the minimum number of shares that would constitute a quorum for the transaction of business at the annual meeting.

The Nominating Committee recommended and the Board of Directors selected the persons named below for election to the Board of Directors. All nominees are currently directors of the Company. If, prior to the Annual Meeting, it should become known that any of the following individuals will be unable to serve as a director after the Annual Meeting by reason of death, incapacity or other unexpected occurrence, the proxies will be voted for such substitute nominee as is selected by the Board of Directors. The Board of Directors has no reason to believe that any of the following nominees will be unable to serve. The election of the nominees requires the affirmative vote by a plurality of the voting power of the shares present and entitled to vote on the election of directors at a meeting at which a quorum is present.

The following table sets forth the principal occupations (for at least the last five years) and directorships of the nominees:

<b>Name</b>	<b>Principal Occupation and Directorships</b>	<b>Age</b>	<b>Director Since</b>
Bradley D. Slye	Chairman of the Board and President of the Company since 1997; Chief Financial Officer since 2000	45	1997
Peter R. Peterson	President, P.R. Peterson Company (a venture capital firm); Secretary of the Company since 1973; Director of PPT Vision, Inc.	71	1969
John S. Strom	Retired; Vice President of Financial Planning & Analysis of Northwest Bancorp (currently Wells Fargo)	71	1989
Joseph A. Marino	President and CEO of Cardia, Inc. (a medical equipment manufacturer) since 1998	53	1994
Geoffrey W. Miller	Controller of Wilcox Paper (a distributor of fine paper to the Printing Industry) since 2002; General Manager of AmSan Brissman Kennedy in 2001 (a distributor of janitorial supplies); CFO/VP Operations of AmSan Brissman Kennedy since 1999	50	1999

**SECURITY OWNERSHIP OF CERTAIN  
BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth information, as of February 21, 2005, regarding the beneficial ownership of the outstanding shares of Common Stock by persons known by the Company to beneficially own more than 5% of the outstanding shares of Common Stock, by directors and director nominees, by the executive officers named in the Summary Compensation Table, and by such directors and executive officers as a group.

Name and Address of Beneficial Owner	Common Stock Number of Shares Beneficially Owned(1)(2)	Percent of Class
Peter R. Peterson 6111 Blue Circle Drive Minnetonka, MN 55343	1,264,551(3)	39.2%
Bradley D. Slye 6111 Blue Circle Drive Minnetonka, MN 55343	247,954(4)	7.4%
John S. Strom 5005 Arden Avenue Edina, MN 55424	16,750(5)	*
Joseph A. Marino 13770 Frontier Court Burnsville, MN 55337	22,500(6)	*
Geoffrey W. Miller 12735 42 <sup>nd</sup> Place North Plymouth, MN 55442	12,000(7)	*
Officers and Directors as a Group	1,563,755(8)	46.0%

\* Indicates ownership of less than one percent (1.0%).

(1) Except as otherwise indicated, each person named or included in the group has the sole power to vote and sole power to direct the disposition of all shares listed as beneficially owned by him/her.

(2) Beneficial ownership information is based on information furnished by the specified persons and is determined in accordance with Rule 13d-3 under the Exchange Act, as required for purposes of this Proxy Statement. Accordingly, it includes shares of Common Stock that are issuable upon the exercise of stock options exercisable within 60 days of February 21, 2005. Such information is not necessarily to be construed as an admission of beneficial ownership for other purposes.

(3) Includes 5,850 shares held by Mr. Peterson's spouse, 11,400 shares held in Keogh Plan and 6,750 shares purchasable upon exercise of options presently exercisable or exercisable within 60 days of February 21, 2005.

(4) Includes 5,190 shares held by Mr. Slye's spouse, 605 shares held by Mr. Slye's children, 16,750 shares held by the ESOP for the account of Mr. Slye, and 133,000 shares purchasable upon exercise of options presently exercisable

or exercisable within 60 days of February 21, 2005.

(5) Includes 15,000 shares purchasable upon exercise of options presently exercisable or exercisable within 60 days of February 21, 2005.

(6) Includes 15,000 shares purchasable upon exercise of options presently exercisable or exercisable within 60 days of February 21, 2005.

(7) Includes 12,000 shares purchasable upon exercise of options presently exercisable or exercisable within 60 days of February 21, 2005.

(8) Includes 181,750 shares that may be purchased by officers and directors upon exercise of options presently exercisable or exercisable within 60 days of February 21, 2005, and 16,750 shares allocated to officers' accounts under the ESOP.

**EXECUTIVE COMPENSATION****Compensation Summary**

The following table summarizes information concerning the compensation awarded or paid to, or earned by, the Company's Chairman and President/Chief Executive Officer during each of the Company's last three fiscal years. No other executive officers received salary and bonus for fiscal 2004 exceeding \$100,000.

**Summary Compensation Table**

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Other Annual Comp (\$)	Restricted Stock Award(s) (\$)	Long-Term Compensation Awards	Payouts	All Other Comp \$(a)
						Securities Underlying Option SARs (#)	LTIP Payouts (\$)	
Bradley D. Slye	2004	176,000	88,000	0	0	75,000	0	10,535
Chairman	2003	176,000	88,000	0	0	0	0	10,520
President, CEO, CFO	2002	176,000	88,000	0	0	0	0	7,775

(a) Amounts reflect allocations to individual's account of Company contributions to the ESOP, 401(k) Plan, and/or standard employee benefit plans

**Stock Options**

The following tables set forth information concerning (1) individual grants of options to purchase Company Common Stock made to the named executive officer(s) during fiscal 2004, and (2) individual exercises of stock options by the named executive officer(s) during fiscal 2004, as well as the number of options outstanding at the end of fiscal 2004 for the named executive officer(s).

**Options/SAR Grants in Last Fiscal Year****Individual Grants**



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Name	Grant Date	Number of Securities Underlying Options/SARs Granted (#)	Percent of Total Options/SARs Granted to Employees in Fiscal Yr	Exercise or Base Price (\$/sh)	Expiration Date
Bradley D. Slye	08/13/2004	75,000(a)	74.3%	4.16000	08/13/2014

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(a) Consists of an incentive stock option granted pursuant to the Company's 1997 Stock Option Plan. The 1997 Stock Option Plan is administered by the Compensation Committee. Subject to the provisions of the 1997 Stock Option Plan, the Compensation Committee designates the persons to be granted options, the type of option, the number of underlying shares, the exercise price, the date of grant, and the date options are first exercisable. This option was granted on the date above at an exercise price equal to 100% of the fair market value of the Common Stock on the date of the grant. The option becomes exercisable in cumulative installments of one-third of the shares, the first being exercisable on the date of the grant, the remaining on the next two anniversaries of the date of grant.

**Aggregated Options/SAR Exercises in Last Fiscal Year And**

**Fiscal Year-End Options/SAR Values (a)**

Name	Shares Acquired on Exercise (#)	Value Realized (\$)	Number of Securities Underlying Unexercised Options/SARs (a) at Fiscal Year-End (#)			Value of Unexercised In-the-Money Options/SARs at Fiscal Year-End (\$)	
			Exercisable	Unexercisable		Exercisable	Unexercisable
Bradley Slye	0	N/A	133,000	50,000	\$	342,425	\$ 208,000

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(a) Consists entirely of stock options.

(a) Consists entirely of stock options.

**SECTION 16(a) BENEFICIAL OWNERSHIP**

**REPORTING COMPLIANCE**

Pursuant to Section 16(a) of the Exchange Act, the Company's directors, its executive officers, and any persons who beneficially own more than 10% of the Company's Common Stock are required to report their initial ownership of Common Stock and subsequent changes in that ownership to the Securities and Exchange Commission. Specific due dates for those reports have been established, and the Company is required to disclose in this Proxy Statement any failure to file by those due dates during fiscal 2004. Based upon a review of such reports furnished to the Company, or written representations that no reports were required, the Company believes that all of those filing requirements were satisfied with respect to fiscal 2004, except that Peter Peterson was late filing one Form 4 reporting one transaction and John Strom was 2 days late filing one Form 4 reporting one transaction.

**APPROVAL OF INDEPENDENT AUDITORS**

**Proposal #3**

The Company's Board of Directors retained Virchow, Krause and Company, LLC as its principal independent auditors for the fiscal year ended December 31, 2004 and has selected Virchow, Krause and Company, LLC to serve as the Company's auditors for the fiscal year ending December 31, 2005. The Board of Directors desires that the selection of such auditors for the current fiscal year be submitted to the shareholders for ratification. If the selection is not ratified, the Board of Directors will reconsider its decision.

A representative of Virchow, Krause & Company, LLC is expected to be present at the Annual Meeting, will have an opportunity to make a statement if he or she desires to do so and will be available to respond to appropriate questions.

On June 24, 2003, the Company dismissed Schweitzer Karon & Bremer, LLC as the Company's independent public accountants. The Company's Board of Directors and audit committee participated in and approved the decision to change accountants.

The reports of Schweitzer Karon & Bremer on the Company's financial statements for the fiscal years ended December 31, 2002 and 2003, contained no adverse opinion or disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope, or accounting principles.

In connection with its audits for the fiscal years ended December 31, 2002 and 2003, and the period through June 24, 2003, there were no disagreements with Schweitzer Karon & Bremer on any matter of accounting principles or practices, financial statement disclosure, auditing scope or procedure, which disagreements if not resolved to the satisfaction of Schweitzer Karon & Bremer would have caused them to make reference thereto in their report on the financial statements for such periods.

**DISCLOSURE OF FEES PAID TO INDEPENDENT AUDITORS****Audit Fees**

The following fees were paid to Schweitzer, Karon & Bremer, LLC ( SKB ) and Virchow, Krause & Company, LLC ( VKC ) for fiscal years 2003 and 2004:

	FY 2004(VKC)	FY 2004 (SKB)	FY 2003 (VKC)	FY 2003 (SKB)
<b>Audit Fees</b>	\$ 53,035	\$ 4,981	\$ 15,270	\$ 2,596
<b>Audit-Related Fees</b>	\$ 0	\$ 0	\$ 0	\$ 650
<b>Tax Fees</b>	\$ 10,775	\$ 0	\$ 0	\$ 0
<b>All Other Fees</b>	\$ 2,694	\$ 0	\$ 0	\$ 7,007

**Audit Fees** were for professional services rendered for the audit of the Company's consolidated financial statements and review of the interim consolidated financial statements included in quarterly reports and services that are normally provided by Virchow, Krause & Company, LLC in connection with statutory and regulatory filings or engagements.

**Audit-Related Fees** were for assurance and related services that are reasonably related to the performance of the audit or review of the Company's consolidated financial statements and are not reported under Audit Fees.

**Tax Fees** were for professional services for federal and state tax compliance, tax advice and tax planning.

**All Other Fees** were for certain financial reporting services in connection with an investment by the company.

Pursuant to its written charter, the Audit Committee is required to pre-approve all audit services, as well as all non-audit services performed by the Company's independent auditors in order to assure that the provision of such non-audit services does not impair the auditor's independence. Unless a particular service has received general pre-approval by the Audit Committee in accordance with the Audit Committee's pre-approval policy, each service provided must be specifically pre-approved. Any proposed services exceeding pre-approved costs levels will require specific pre-approval by the Audit Committee.

As part of the Company's annual engagement agreement with its independent auditor, the Audit Committee pre-approves the following audit services to be provided by the independent auditor: statutory and financial audits for the company and any of its subsidiaries and affiliates, audit services associated with SEC registration statements, periodic reports and other documents filed with the SEC, production of other documents issued by the independent auditor in connection with securities offerings (e.g., comfort letters, consents), and assistance in responding to SEC

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comment letters. The Audit Committee also provides pre-approval in the annual engagement of most consulting services provided by the independent auditor related to the accounting or disclosure treatment of transactions or events and the actual or potential impact of final or proposed rules, standards or interpretations by the SEC, FASB, or other regulatory or standard-setting bodies.

The Audit Committee has also provided the Company's independent auditors with a general pre-approval of certain non-audit services, primarily tax services. The Audit Committee does not believe that performance of these tax services impairs the auditor's independence. Specifically, the Audit Committee has given the independent auditors pre-approval for U.S. federal, state, and local tax planning and advice, U.S. federal, state, and local tax compliance, international tax planning and advice, international tax compliance, and tax planning and advice related to merger and acquisition activities. The Company's independent auditors must inform the Audit Committee whenever a pre-approved service is provided. The aggregate amount of fees for these pre-approved tax services may not exceed \$8,000 without explicit approval by the Audit Committee.

The term of any pre-approval is 12 months from the date of pre-approval, unless the Audit Committee specifically provides for a different term. The Audit Committee retains the right to periodically revise the above list of pre-approved services.



## AUDIT COMMITTEE REPORT

The Board of Directors maintains an Audit Committee comprised of three of the Company's outside directors. The Board of Directors and the Audit Committee believe that the Audit Committee's current member composition satisfies the rule of the National Association of Securities Dealers, Inc. ( NASD ) that governs audit committee composition, Rule 4350(d)(2), including the requirement that audit committee members all be independent directors as that term is defined by NASD Rule 4200(a)(15).

The Audit Committee of the Board of Directors oversees and monitors the participation of the Company's management and independent auditors throughout the financial reporting process.

In connection with its function to oversee and monitor the financial reporting process of the Company, the Audit Committee has done the following:

Reviewed and discussed the audited financial statements for the fiscal year ended December 31, 2004 with the Company's management;

Discussed with the Company's independent auditors those matters required to be discussed by SAS 61 (Codification of Statements on Auditing Standards, AU §380); and

Received the written disclosure and the letter from the independent auditors required by Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees) and has discussed with the independent auditors its independence.

Based on the foregoing, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in the Company's annual report on Form 10-KSB for the fiscal year ended December 31, 2004.

### Audit Committee

*John S. Strom*

*Joseph A. Marino*

*Geoffrey W. Miller*

#### **OTHER MATTERS**

The Board of Directors knows of no other matters to be brought before the Annual Meeting. However, if any other matters are properly brought before the Annual Meeting, it is the intention of the persons named in the accompanying proxy to vote in accordance with their judgment on such matters.

#### **SHAREHOLDER PROPOSALS**

Shareholder proposals for the 2006 Annual Meeting of Shareholders of the Company must be received no later than November 25, 2005 at the Company's principal executive offices, 6111 Blue Circle Drive, Minnetonka, Minnesota 55343, directed to the attention of the P. R. Peterson, Corporate Secretary, in order to be considered by the Board of Directors for inclusion in next year's annual meeting proxy material under the SEC's proxy rules.

Also, if a shareholder proposal intended to be presented at the next annual meeting but not included in the Company's proxy statement and proxy is received by the Company after February 8, 2006, then management named in the Company's proxy form for the next annual meeting will have discretionary authority to vote shares represented by such proxies on the shareholder proposal, if presented at the meeting, without including information about the proposal in the Company's proxy material.

#### **FORM 10-KSB**

A copy of the Company's Annual Report to the Securities and Exchange Commission on Form 10-KSB for the fiscal year ended December 31, 2004 has been provided with this Proxy Statement. The Company will furnish to any shareholder, upon written request, any exhibit described in the list accompanying the Form 10-KSB upon the payment, in advance, of reasonable fees related to the Company's furnishing such exhibits(s). Any such request should include a representation that the shareholder was the beneficial owner of shares of Electro-Sensors Common Stock on February 21, 2005, the record date for the 2005 Annual Meeting, and should be directed to Mr. Bradley Slye, Chief Executive Officer, at the Company's principal address.

**The foregoing Notice of Annual Meeting and Proxy Statement are sent by order of the Board of Directors.**

BRADLEY D. SLYE

President

March 25, 2005

**ELECTRO-SENSORS, INC.**

**THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS.**

**PROXY FOR ANNUAL MEETING**

**April 20, 2005**

The undersigned hereby appoints BRADLEY D. SLYE and PETER R. PETERSON, and each of them, with full power of substitution, his or her Proxies to represent and vote, as designated below, all shares of the Common Stock of Electro-Sensors Inc. registered in the name of the undersigned at the Annual Meeting of Shareholders of the Company to be held at the Sheraton Bloomington, 7800 Normandale Boulevard, Bloomington, Minnesota, at 2:00 p.m. local time, on April 20, 2005, and at any adjournment thereof. The undersigned hereby revokes all proxies previously granted with respect to such meeting.

**THIS PROXY WHEN PROPERLY EXECUTED WILL BE VOTED AS DIRECTED OR, IF NO DIRECTION IS GIVEN FOR A PARTICULAR PROPOSAL, WILL BE VOTED FOR SUCH PROPOSAL.**

***DETACH BELOW AND RETURN USING THE ENVELOPE PROVIDED***

**ELECTRO-SENSORS, INC. 2005 ANNUAL MEETING**

**The Board of Directors recommends that you vote FOR each proposal.**

1. Set number of directors at five
  2. Elect five directors:            1   B. Slye            2   P. Peterson            3   G. Miller            4   J.  
Marino            5   J. Strom
  3. Approve appointment of Virchow, Krause & Company, LLC as independent auditors for the current fiscal year.
  4. Other Matters. In their discretion, the Proxies are authorized to vote upon such other business as may properly come before the meeting.
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