

TAITRON COMPONENTS INC
Form 10QSB
November 14, 2005

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

FORM 10-QSB

ý QUARTERLY REPORT UNDER SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2005

“TRANSITION REPORT UNDER SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 0-25844

TAITRON COMPONENTS INCORPORATED

(Exact name of small business issuer as specified in its charter)

California
(State or Other Jurisdiction of
Incorporation or Organization)

95-4249240
(I.R.S. Employer
Identification No.)

28040 West Harrison Parkway
Valencia, California 91355-4162
(Address Of Principal Executive Offices)

(661) 257-6060
(Issuer's Telephone Number)

NONE
(Former Name, Address and Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 No

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

Class
Class A Common Stock, \$.001 par value

Outstanding on October 31, 2005
4,700,145

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Class B Common Stock, \$.001 par value

762,612

Transitional Small Business Disclosure Format (check one): Yes No

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

TAITRON COMPONENTS INCORPORATED

Condensed Consolidated Balance Sheets

(Dollars in Thousands)

| Assets | September 30, 2005 |
|--|-------------------------------|
| | (Unaudited) |
| Current assets: | |
| Cash and cash equivalents | \$ 1,466 |
| Trade accounts receivable, net | 1,500 |
| Inventory, net | 16,991 |
| Prepaid expenses and other current assets | 186 |
| Total current assets | 20,143 |
| Property and equipment, net | 4,463 |
| Other assets | 79 |
| Total assets | \$ 24,685 |
| Liabilities and Shareholders' Equity | |
| Current liabilities: | |
| Trade accounts payable | \$ 838 |
| Accrued liabilities and other | 556 |
| Total current liabilities | 1,394 |
| Total liabilities | 1,394 |
| Commitments and contingencies (Note 3) | |
| Shareholders' equity: | |
| Preferred stock, \$.001 par value. Authorized 5,000,000 shares. None issued or outstanding. | - |
| Class A common stock, \$.001 par value. Authorized 20,000,000 shares; issued and outstanding 4,700,145 shares. | 5 |
| Class B common stock, \$.001 par value. Authorized, issued and outstanding 762,612 shares. | 1 |
| Additional paid-in capital | 10,416 |
| Accumulated other comprehensive loss, net of tax | (18) |
| Retained earnings | 12,887 |
| Total shareholders' equity | 23,291 |
| Total liabilities and shareholders' equity | \$ 24,685 |

See accompanying notes to condensed consolidated financial statements.

TAITRON COMPONENTS INCORPORATED

Condensed Consolidated Statements of Operations

(Dollars in thousands, except per share amounts)

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|---|-------------|--|-------------|
| | 2005 | 2004 | 2005 | 2004 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| Net sales | \$ 2,288 | \$ 2,371 | \$ 6,332 | \$ 7,509 |
| Cost of goods sold | 1,625 | 1,665 | 4,582 | 5,395 |
| Gross profit | 663 | 706 | 1,750 | 2,114 |
| Selling, general and administrative expenses | 706 | 636 | 1,952 | 1,907 |
| (Loss) income from operations | (43) | 70 | (202) | 207 |
| Interest income (expense), net | 6 | (44) | (11) | (160) |
| Other income (expense), net | 22 | 3 | 61 | 16 |
| (Loss) income before income taxes | (15) | 29 | (152) | 63 |
| Income tax provision | (8) | - | (8) | - |
| Net (loss) income | \$ (23) | \$ 29 | \$ (160) | \$ 63 |
| (Loss) income per share | | | | |
| Basic | \$ (.00) | \$.01 | \$ (.03) | \$.01 |
| Diluted | \$ (.00) | \$.01 | \$ (.03) | \$.01 |
| Weighted average common shares outstanding | | | | |
| Basic | 5,462,757 | 5,460,258 | 5,461,952 | 5,466,463 |
| Diluted | 5,462,757 | 6,044,258 | 5,461,952 | 6,037,463 |

See accompanying notes to condensed consolidated financial statements.

TAITRON COMPONENTS INCORPORATED
Condensed Consolidated Statements of Cash Flows

(Dollars in thousands)

| | Nine months ended September 30, | |
|--|--|-------------|
| | 2005 | 2004 |
| | (Unaudited) | (Unaudited) |
| Cash flows from operating activities: | | |
| Net (loss) income | \$ (160) | \$ 63 |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: | | |
| Depreciation and amortization | 173 | 193 |
| Amortization of debt discount related to options issued with notes payable | - | 28 |
| Provision for sales returns and doubtful accounts | 92 | 27 |
| Gain on sale of assets | - | (6) |
| Changes in assets and liabilities: | | |
| Trade accounts receivable | (493) | (139) |
| Inventory, net | 1,250 | 1,387 |
| Prepaid expenses and other current assets | 231 | (135) |
| Other assets | (15) | (1) |
| Trade accounts payable | 32 | 51 |
| Accrued liabilities and other | 165 | 3 |
| Total adjustments | 1,435 | 1,408 |
| Net cash provided by operating activities | 1,275 | 1,471 |
| Cash flows from investing activities: | | |
| Acquisitions of property and equipment | (3) | (32) |
| Proceeds from sale of assets | - | 6 |
| Net cash used by investing activities | (3) | (26) |
| Cash flows from financing activities: | | |
| Payments on notes payable | (1,326) | (2,699) |
| Repurchase of Class A Common Stock | - | (322) |
| Proceeds from exercise of stock options and issuance of stock | 2 | 27 |
| Net cash used in financing activities | (1,324) | (2,994) |
| Impact of exchange rate changes on cash | (21) | 4 |
| Net decrease in cash and cash equivalents | (73) | (1,545) |
| Cash and cash equivalents, beginning of period | 1,539 | 2,953 |
| Cash and cash equivalents, end of period | \$ 1,466 | \$ 1,408 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest | \$ 48 | \$ 154 |
| Cash paid for income taxes | \$ 10 | \$ 30 |

TAITRON COMPONENTS INCORPORATED
Notes to Condensed Consolidated Financial Statements
September 30, 2005
(All amounts are unaudited)

Note 1 - Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Taitron Components Incorporated (“the Company”) were prepared in accordance with accounting principles generally accepted in the United States of America and reflect all adjustments, consisting of normal recurring accruals and adjustments, which are, in the opinion of management, necessary for a fair presentation of the consolidated financial position and results of operations at and for the periods presented. Such financial statements do not include all the information or footnotes necessary for a complete presentation and, accordingly, should be read in conjunction with the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2004, and the notes thereto, which include significant accounting policies and estimates. The results of operations for the interim periods are not necessarily indicative of results for the full year.

Note 2 - Summary of Significant Accounting Policies and Estimates

Principles of Consolidation

The unaudited condensed consolidated financial statements include the accounts of the Company and its majority-owned subsidiary. All significant intercompany transactions and balances have been eliminated in consolidation.

Revenue Recognition

Revenue is typically recognized upon shipment of merchandise and sales are recorded net of discounts, rebates, and returns. Reserves for sales allowances and customer returns are established based upon historical experience and management’s estimates as shipments are made. Sales returns for the quarters ended September 30, 2005 and 2004 were \$31,000 and \$30,000, respectively, and for the nine months ended September 30, 2005 and 2004 aggregated \$92,000 and \$83,000, respectively.

Allowance for Sales Returns and Doubtful Accounts

On a case-by-case basis, the Company accepts returns of products from its customers, without restocking charges, when they can demonstrate an acceptable cause for the return. Requests by a distributor to return products purchased for its own inventory generally are not included under this policy. The Company will, on a case-by-case basis, accept returns of products upon payment of a restocking fee, which is generally 15% to 30% of the net sales price. The Company will not accept returns of any products that were special-ordered by a customer or that otherwise are not generally included in inventory. The allowance for sales returns and doubtful accounts at September 30, 2005 aggregated \$64,000.

Inventory

Inventory, consisting principally of products held for resale, is recorded at the lower of cost (determined using the first in-first out method) or estimated market value. Inventory is presented net of valuation allowances of \$1,371,000 at September 30, 2005.

Income Taxes

The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which the 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. Valuation allowances are recorded, when necessary, to reduce deferred tax assets to the amount expected to

be realized. The Company has fully reserved against its deferred income tax assets, as management could not determine that it was more likely than not such assets would be realized.

(Loss) Income Per Share

Basic (loss) income per share is computed by dividing net (loss) income available to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted income per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. Common equivalent shares for both the quarter and nine months ended September 30, 2005, of approximately 616,000 and 603,000, respectively, are excluded from the computation of diluted (loss) per share as their effect is anti-dilutive.

Stock Option Plan

The Company has adopted the disclosure requirements of SFAS No. 148, "Accounting for Stock-Based Compensation—Transition and Disclosure". SFAS No. 123 allows companies to choose whether to account for employee stock-based compensation on a fair value method, or to continue to account for stock-based compensation under the current intrinsic value method as prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees." The Company has elected to continue to follow the provisions of APB Opinion No. 25. SFAS No. 148 requires interim disclosures regarding the pro forma effects of compensation expense had stock options issued under the Company's 1995 Stock Incentive Plan been determined based on the fair value consistent with SFAS No. 123.

Accordingly, under SFAS No. 123, the Company's net earnings (loss) and diluted earnings (loss) per share for the quarters and nine months ended September 30, 2005 and 2004, would have been changed to the pro forma amounts indicated below:

| | Three Month Period Ended September 30, | | Nine Month Period Ended September 30, | |
|---|---|-----------|--|-----------|
| | 2005 | 2004 | 2005 | 2004 |
| Net (loss) income As reported | \$ (23,000) | \$ 29,000 | \$ (160,000) | \$ 63,000 |
| Pro Forma | \$ (17,000) | \$ 36,000 | \$ (142,000) | \$ 84,000 |
| Diluted (loss) income per share As reported | \$ - | \$ 0.01 | \$ (0.03) | \$ 0.01 |
| Pro Forma | \$ - | \$ 0.01 | \$ (0.03) | \$ 0.01 |

The Company's 1995 Stock Incentive Plan expired by its terms in March 2005. Since no new grants can be awarded out of this plan, the total weighted average fair value of options granted for the quarter and nine months ended September 30, 2005 was \$0. At September 30, 2005, the number of options exercisable was 616,000 and the weighted average exercise price of those options was \$1.74.

Reclassification

Certain amounts in the 2004 condensed consolidated financial statements have been reclassified to conform with the 2005 presentation.

Use of Estimates

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States. These estimates have a significant impact on the Company's valuation and reserve accounts relating to the allowance for sales returns, doubtful accounts, inventory reserves and deferred income taxes. Actual results could differ from these estimates.

Note 3 - Commitments and Contingencies

On July 9, 2005, the Company renewed its revolving line of credit facility providing up to \$3 million for operating purposes. The agreement governing this credit facility contains security agreements covering essentially all assets of the Company and financial covenants requiring compliance with certain financial ratios. As of the date of this report, the Company has not yet used this credit facility.

Effective July 1, 2006, the European Union (“EU”) will begin restricting the distribution of products within the EU containing certain substances, including lead. At the present time, much of our inventory contains substances prohibited by the RoHS directive and we believe it is likely that we will not be able to distribute non-RoHS compliant products to most customers who intend to sell their finished goods in the EU after the effective date. Upon effectiveness of the RoHS legislation, some of our inventory may become obsolete and unsaleable and, as a result, have to be written off. See Item 2 - “Management’s Discussion and Analysis - Critical Accounting Policies - *Impact of Governmental Regulation*.”

Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the condensed consolidated financial statements, including the related notes, appearing in Item 1 of this report as well as our most recent annual report on Form 10-KSB for the year ended December 31, 2004. Also, several of the matters discussed in this document contain forward-looking statements that involve risks and uncertainties. Forward-looking statements usually are denoted by words or phrases such as “believes,” “expects,” “projects,” “estimates,” “anticipates,” “will likely result” or similar expressions. We wish to caution readers that all forward-looking statements are necessarily speculative and not to place undue reliance on forward-looking statements, which speak only as of the date made, and to advise readers that actual results could vary due to a variety of risks and uncertainties. Factors associated with the forward looking statements that could cause the forward looking statements to be inaccurate and could otherwise impact our future results are set forth in detail in our most recent annual report on Form 10-KSB. In addition to the other information contained in this document, readers should carefully consider the information contained in our most recent annual report on Form 10-KSB under the heading “Cautionary Statements and Risk Factors.”

References to “Taitron,” “the Company,” “we,” “our” and “us” refer to Taitron Components Incorporated and its majority-owned subsidiary, unless the context otherwise requires.

Critical Accounting Policies and Estimates

Use Of Estimates - Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare its condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States. These estimates have a significant impact on the Company’s valuation and reserve accounts relating to the allowance for sales returns, doubtful accounts, inventory reserves and deferred income taxes. Actual results could differ from these estimates.

Revenue Recognition - Revenue is recognized upon shipment of the merchandise, which is when legal transfer of title occurs. Reserves for sales allowances and customer returns are established based upon historical experience and our estimates of future returns. Sales returns for the quarters ended September 30, 2005 and 2004 were \$31,000 and \$30,000, respectively, and for the nine months ended September 30, 2005 and 2004 aggregated \$92,000 and \$83,000, respectively. The allowance for sales returns and doubtful accounts at September 30, 2005 aggregated \$64,000.

Inventory - Inventory, consisting principally of products held for resale, is recorded at the lower of cost (determined using the first in-first out method) or estimated market value. We had inventory balances in the amount of \$16,991,000 at September 30, 2005, which is presented net of valuation allowances of \$1,371,000. We evaluate inventories to identify excess, high-cost, slow-moving or other factors rendering inventories as unmarketable at normal profit margins. For inventories supplied under franchise agreements, we rely upon our contractual rights to receive compensation for price differences caused by market fluctuations. Due to the large number of transactions

and the complexity of managing and maintaining a large inventory of product offerings, estimates are made regarding adjustments to the cost of inventories. Based on our assumptions about future demand and market conditions, inventories are carried at the lower of cost or estimated market value. If our assumptions about future demand change, or market conditions are less favorable than those projected, additional write-downs of inventories may be required. In any case, actual amounts could be different from those estimated.

Impact of Governmental Regulation - Our worldwide operations are subject to local laws and regulations. As such, of particular interest is the European Union ("EU") directive relating to the Restriction of Certain Hazardous Substance ("RoHS"). Effective July 1, 2006, this directive restricts the distribution of products within the EU containing certain substances, including lead. While the enabling legislation of a number of EU member countries has not yet been adopted, we believe it is likely that we will not be able to distribute non-RoHS compliant products to most customers who intend to sell their finished goods in the EU after the effective date. At the present time, much of our inventory contains substances prohibited by the RoHS directive. Further, many of our suppliers are not yet supplying RoHS compliant products. Upon effectiveness of the RoHS legislation, some of our inventory may become obsolete and unsaleable and, as a result, have to be written off. While we are working closely with our customers and suppliers to minimize this impact, at this time, it is difficult to quantify the financial impact, if any, of such obsolete inventory.

Deferred Taxes - We review the nature of each component of our deferred income taxes for reasonableness. If determined that it is more likely than not that we will not realize all or part of our net deferred tax assets in the future, we record a valuation allowance against the deferred tax assets, which allowance will be charged to income tax expense in the period of such determination. We also consider the scheduled reversal of deferred tax liabilities, tax planning strategies and future taxable income in assessing the realizability of deferred tax assets. We also consider the weight of both positive and negative evidence in determining whether a valuation allowance is needed. Based upon recent operating results and the difficulty of estimating future market conditions, we have fully reserved a \$669,000 allowance against our net deferred tax assets.

Recent Accounting Policies

In December 2004, the FASB issued SFAS No. 123 (R), "Share-Based Payment" ("SFAS 123(R)") which establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. This SFAS 123(R) standard requires that the fair value of such equity instruments be recognized as expense in the historical financial statements as services are performed. Prior to SFAS 123(R), only certain pro forma disclosures of fair value were required. SFAS 123(R) shall be effective for small business issuers as of the beginning of the first interim or annual reporting period that begins after December 15, 2005. The adoption of this new accounting pronouncement may have a material impact on our financial statements during the next year ended December 31, 2006.

Overview

We are a national distributor of electronic components, primarily focused on transistors, diodes and other discrete semiconductors, optoelectronic devices and passive components with a reputation of in-depth inventories and knowledge of the products we sell. Our customers consist of other electronic distributors, contract electronic manufacturers (CEMs) and original equipment manufacturers (OEMs).

We believe that demand for discrete semiconductors in the U.S. market had drastically declined since 2000. This declining demand has resulted from the accelerated trend of moving the production capacity of OEM/CEM customers abroad and the consolidation of CEM customers domestically. In response, we are refocusing our business strategy beyond the traditional role of electronic components fulfillment to the additional role of engineering and turn-key services for our existing OEM and CEM customers by outsourcing their product design and manufacturing work offshore. We formed some strategic business partnerships with a few customers and are providing them with original

design and manufacturing (ODM) services for their multi-year turn-key projects. We expect to see some more opportunities and results from these additional services during 2006.

Our core strategy of electronic components fulfillment, however, consists of carrying a substantial quantity and variety of products in inventory to meet the rapid delivery requirements of our customers. This strategy allows us to fill customer orders immediately from stock on hand. Although we believe better market conditions may

return, we are focused on lowering our inventory balances and increasing our cash holdings. Our long-term strategy is to rely not only on our core strategy of component fulfillment service, but also the value-added engineering and turn-key services. In accordance with Generally Accepted Accounting Principles, we classify inventory as a current asset. However, if all or a substantial portion of the inventory was required to be immediately liquidated, the inventory would not be as readily marketable or liquid as other items included or classified as a current asset, such as cash. We cannot assure you that demand in the discrete semiconductor market will increase and that market conditions will improve. Therefore, it is possible that further declines in our carrying values of inventory may result.

Results of Operations

Three month Period Ended September 30, 2005 Compared To The Three month Period Ended September 30, 2004.

Net sales for the three months ended September 30, 2005 were \$2,288,000, compared with \$2,371,000 for the same period last year, a decrease of \$83,000 or 3.5%. The decrease is primarily due to a decrease in demand for our discrete and passive and semiconductor components.

Cost of goods sold for the quarter ended September 30, 2005 decreased to \$1,625,000 from \$1,665,000 for the same period last year, a decrease of \$40,000 or 2.4%. Consistent with the decrease in net sales, cost of goods sold decreased. Gross profit decreased as a percentage of net sales to 29% for the quarter ended September 30, 2005 from 29.8% for the same period last year. Gross profit decreased by \$43,000 to \$663,000 for the quarter ended September 30, 2005 from \$706,000 for the same period in 2004.

Selling, general and administrative (“SG&A”) expenses increased by \$70,000 or 11% for the quarter ended September 30, 2005 compared to the same period of 2004. The increase is primarily attributable to higher outside professional related expenses by \$44,000 and the reduction of bad debt reserves by \$30,000 in the prior period. The corresponding average employee base declined to 23 from 28 employees, which represents a 17.9% reduction in overall workforce. As a percentage of net sales, SG&A increased to 30.9% from 26.8% for the three months ended September 30, 2005 and 2004, respectively.

Operating loss was \$43,000 for the quarter ended September 30, 2005 as compared to an operating income of \$70,000 for the same period last year. Operating results decreased primarily from lower gross profits and higher SG&A, as discussed above.

Interest expense, net of interest income, for the quarter ended September 30, 2005 decreased by \$50,000 compared to the same period last year. The decrease is primarily due to lower outstanding borrowing levels during the current quarter, when compared to the same period last year.

Income tax provision was \$8,000 during the quarter ended September 30, 2005 as compared to \$0 for the same period last year.

Net loss was \$23,000 for the quarter ended September 30, 2005 as compared with \$29,000 net income for the same period last year.

Nine month Period Ended September 30, 2005 Compared To The Nine month Period Ended September 30, 2004.

Net sales for the nine months ended September 30, 2005 were \$6,332,000 compared with net sales for the nine months ended September 30, 2004 of \$7,509,000, a decrease of \$1,177,000 or 15.7%.

Cost of goods sold decreased by \$813,000 to \$4,582,000 for the nine months ended September 30, 2005, a decrease of 15.1% from the same period in 2004. Consistent with the decrease in net sales, cost of goods sold decreased, however at a slower rate, resulting in gross profit decreasing as a percentage of net sales to 27.6% for the first nine months of this year from 28.2% for the same period last year. Gross profit decreased by \$364,000 to \$1,750,000 for the nine months ended September 30, 2005 from \$2,114,000 for the same period in 2004.

SG&A expenses increased by \$45,000 or 2.4% for the nine months ended September 30, 2005 compared to the same period in 2004. The increase is primarily attributable to higher outside professional related expenses by \$81,000 and the reduction of bad debt reserves by \$56,000 in the prior period, offset with lower personnel related

expenses by \$24,000, lower depreciation and amortization by \$18,000, lower trade commission fees by \$15,000 and lower public company expenses by \$27,000. As a percentage of net sales, SG&A increased to 30.8% for the nine months ended September 30, 2005 from 25.4% for the same period last year.

Operating loss was \$202,000 for the nine months ended September 30, 2005 as compared to operating income \$207,000 for the same period ended September 30, 2004. Operating results decreased primarily from lower gross profits and higher SG&A expenses, as discussed above.

Interest expense, net of interest income for the nine months ended September 30, 2005 decreased by \$149,000 compared to the nine months ended September 30, 2004. The decrease is primarily due to lower outstanding borrowing levels incurred during the current quarter, when compared to the same period last year.

Income tax provision was \$8,000 for the nine months ended September 30, 2005 as compared to \$0 for the same period ended September 30, 2004.

Net loss was \$160,000 for the nine months ended September 30, 2005 compared to a net income of \$63,000 for the same period in 2004, a decrease of \$223,000 resulting from the same reasons discussed above.

Liquidity and Capital Resources

We have satisfied our liquidity requirements principally through cash generated from operations, short-term commercial loans, subordinated promissory notes and issuance of equity securities. A summary of our cash flows resulting from our operating, investing and financing activities for the nine months ended September 30, 2005 and 2004 are as follows:

| (Dollars in thousands) | Nine months ended September 30, | |
|------------------------|--|-------------|
| | 2005 | 2004 |
| | (Unaudited) | (Unaudited) |
| Operating activities | \$ 1,275 | \$ 1,471 |
| Investing activities | (3) | (26) |
| Financing activities | (1,324) | (2,994) |

Cash flows provided by operating activities decreased to \$1,275,000 during the nine months ended September 30, 2005, as compared to \$1,471,000 during the same period last year. The overall decrease was affected by a decrease in inventory of \$1,250,000 during the first nine months of 2005, as compared to a decrease of \$1,387,000 during the same period last year. The Company's ability to continue generating cash from operations is dependent upon using its current inventory (as opposed to new purchases of inventory) for generating sales, collection of its receivables and extended payments of accounts payables.

Cash flows used in investing activities was \$3,000 during the nine months ended September 30, 2005 compared with \$26,000 during the same period last year.

Cash flows used in financing activities decreased to \$1,324,000 from \$2,994,000 during the nine months ended September 30, 2005 and 2004, respectively. The decrease was primarily the result of using operating cash flow of \$322,000 for repurchase of Class A Common Stocks and \$2,699,000 for repayments of notes payable during the 2004 period.

Inventory is included in current assets; however, it will take over one year for the inventory to turn. Hence, inventory would not be as readily marketable or liquid as other items included in current assets, such as cash.

We believe that funds generated from operations, in addition to existing cash balances, and the revolving line of credit facility is likely to be sufficient to finance our working capital and capital expenditure requirements for the foreseeable future. If these funds are not sufficient, we may secure new sources of asset-based lending on accounts receivables or issue debt or equity securities. Otherwise, we may need to liquidate assets to generate the necessary working capital.

As of the date of this Report, we had no commitments for other equity or debt financing or other capital expenditures.

Item 3. Controls and Procedures

The Company's management, including its Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) as of the end of the reporting period covered by this quarterly report. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this quarterly report, the Company's disclosure controls and procedures are effective such that material information required to be disclosed by the Company (including its consolidated subsidiary) in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified by the Securities and Exchange Commission's rules and forms relating to the Company.

During the period covered by this report, there have been no changes to the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

None.

Item 2. Changes In Securities and Small Business Issuer Purchases of Equity Securities.

There were no issuances or sales of our securities by us during the third quarter of 2005 that were not registered under the Securities Act.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

- a. Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- b. Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

TAITRON COMPONENTS
INCORPORATED

Date: November 14, 2005

By: /s/ Stewart Wang
Stewart Wang
Chief Executive Officer, President,
Chief Financial Officer and Director
(Principal Executive, Financial and Accounting Officer)