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SENSOR SYSTEM SOLUTIONS INC
Form 10QSB
May 26, 2006

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934

For the quarterly period ended March 31, 2006

or

Transition Report Pursuant to Section 13 of 15(d) of the Securities
Exchange Act of 1934

FOR THE TRANSITION PERIOD FROM _____ TO _____

Commission File number 0-024828

SENSOR SYSTEM SOLUTIONS, INC.

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

NEVADA
(State or other jurisdiction of
incorporation or organization)

98-0204898
(IRS Employer Identification No.)

45 Parker Avenue, Suite A
Irvine, California 92618

(Address of principal executive offices)

(949) 855-6688

(Issuer's telephone number)

Check 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 No

As of May 15, 2006 there were 76,586,112 shares of Common Stock outstanding.

TRANSITIONAL SMALL BUSINESS DISCLOSURE FORMAT

Yes No

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
As of March 31, 2006 (Unaudited)
and December 31, 2005

ASSETS

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| | March 31, 2006 (Unaudited) | Dec |
|---|-------------------------------|-------|
| CURRENT ASSETS | ----- | ----- |
| Cash | \$ 38,038 | \$ |
| Accounts receivable | 416,851 | |
| Inventory | 254,127 | |
| Prepays and other current assets | 9,900 | |
| | ----- | ----- |
| Total current assets | 718,916 | |
| Property and equipment, net | 151,167 | |
| Other assets | 104,112 | |
| | ----- | ----- |
| Total assets | \$ 974,195 | \$ |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' DEFICIENCY | | |
| CURRENT LIABILITIES | | |
| Accounts payable and accrued expenses | \$ 1,331,136 | \$ |
| Notes payable | 1,228,564 | |
| Notes payable, related parties | 376,025 | |
| Current portion of capital lease obligations | 9,163 | |
| Current portion of deferred rent concession | 6,000 | |
| | ----- | ----- |
| Total current liabilities | 2,950,888 | |
| | ----- | ----- |
| LONG-TERM LIABILITIES | | |
| Non-current portion of notes payable | 26,656 | |
| Capital lease obligations, net of current portion | 22,921 | |
| Deferred rent concession, net of current portion | 2,272 | |
| | ----- | ----- |
| | 51,849 | |
| | ----- | ----- |
| Commitments and contingencies | | |
| STOCKHOLDERS' DEFICIENCY | | |
| Preferred stock, \$.001 par value, 20,000,000 shares authorized, none outstanding | -- | |
| Common stock, \$.001 par value, 180,000,000 shares authorized, 76,244,112 and 61,705,019 shares issued and outstanding | 76,244 | |
| Common stock to be issued (71,875 and 14,479,093 shares) | 20,594 | |
| Additional paid-in capital | 16,135,735 | 1 |
| Deferred compensation | -- | |
| Accumulated deficit | (18,261,115) | (1 |
| | ----- | ----- |
| Total stockholders' deficiency | (2,028,542) | (|
| | ----- | ----- |
| Total liabilities and stockholders' deficiency | \$ 974,195 | \$ |
| | ===== | ===== |

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 For the three months ended March 31, 2006 and 2005 (Unaudited)

| | 2006 | 2005 |
|--|--------------|--------------|
| Sales, net | \$ 530,098 | \$ 205,015 |
| Cost of goods sold | 332,993 | 147,274 |
| Gross profit | 197,105 | 57,741 |
| Operating expenses | 544,817 | 330,555 |
| Amortization of discount on notes payable | 132,448 | 155,121 |
| Stock-based compensation costs | 60,029 | -- |
| Total operating expenses | 737,294 | 485,676 |
| Gain on sale of equipment to related party | 16,905 | -- |
| Net loss | \$ (523,284) | \$ (427,935) |
| Loss per common share, basic and diluted | \$ (.01) | \$ (.01) |
| Weighted average shares outstanding, basic and diluted | 66,228,292 | 59,279,241 |

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
 CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' DEFICIENCY
 For the three months ended March 31, 2006 (Unaudited)

| | Common Stock | | Common Stock to be issued | | Additional paid-in capital | Deferen compens |
|----------------------------|--------------|-----------|---------------------------|------------|----------------------------------|--------------------|
| | Shares | Amount | Shares | Amount | | |
| Balance January 1, 2006 | 61,705,019 | \$ 61,705 | 14,479,093 | \$ 550,000 | \$15,456,834 | \$ (26, |

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| | | | | | | |
|--|------------|-----------|--------------|-----------|--------------|-------|
| Cancellation of stock options | -- | -- | -- | -- | (26,598) | 26, |
| Stock option expense | -- | -- | -- | -- | 22,635 | |
| Compensatory stock issued | 60,000 | 60 | -- | -- | 16,740 | |
| Warrants issued with notes payable | -- | -- | -- | -- | 130,603 | |
| Common stock issued for exercise of warrants | 14,479,093 | 14,479 | (14,479,093) | (550,000) | 535,521 | |
| Compensatory stock to be issued | -- | -- | 71,875 | 20,594 | -- | |
| Net loss | -- | -- | -- | -- | -- | |
| Balance March 31, 2006 | 76,244,112 | \$ 76,244 | 71,875 | \$ 20,594 | \$16,135,735 | \$ |
| | ===== | ===== | ===== | ===== | ===== | ===== |

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For three months ended March 31, 2006 and 2005 (Unaudited)

| | 2006 | 2005 |
|---|--------------|--------------|
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net loss | \$ (523,284) | \$ (423,284) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Stock-based compensation costs | 60,029 | 20,400 |
| Depreciation and amortization | 20,400 | 15,000 |
| Amortization of discount on notes payable | 132,448 | 15,000 |
| Amortization of deferred compensation | -- | 1,000 |
| Gain on sale of property and equipment | (16,905) | -- |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (186,411) | (3,000) |
| Inventory | 48,044 | -- |
| Prepays and other current assets | 36,734 | 1,000 |
| Deferred rent | (1,500) | (1,000) |
| Accounts payable and accrued expenses | 22,002 | 2,000 |
| Net Cash Used In Operating Activities | (408,443) | (213,284) |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Proceeds from sale of property and equipment | 79,200 | -- |
| | ----- | ----- |

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| | | |
|---|-----------|-------|
| Cash flows from financing activities: | | |
| Proceeds from notes payable | 400,000 | 25 |
| Principal payments on notes payable | (203,336) | |
| Principal payments on capital leases | (2,115) | (|
| | ----- | ----- |
| Net Cash Provided By Financing Activities | 194,549 | 24 |
| | ----- | ----- |
| Net (decrease) increase in cash and cash equivalents | (134,694) | 3 |
| Cash and cash equivalents, beginning of period | 172,732 | 1 |
| | ----- | ----- |
| Cash and cash equivalents, end of period | \$ 38,038 | \$ 4 |
| | ===== | ===== |
| Supplemental disclosure of cash flow information Cash paid for: | | |
| Interest | \$ 6,762 | \$ |
| | ===== | ===== |
| Taxes | \$ -- | \$ |
| | ===== | ===== |
| Non-cash investing and financing activities: | | |
| Cancellations and forfeitures of stock options | \$ 26,598 | \$ 9 |
| Accrued interest added to notes payable principal | 4,000 | 5 |
| Discount related to warrants and convertible notes | 130,603 | 16 |
| Exercise of warrants for debt outstanding | -- | 26 |
| Conversion of notes payable | -- | 31 |

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEMS SOLUTIONS, INC.
CONDENSED NOTES TO FINANCIAL STATEMENTS
FOR THREE MONTHS ENDED MARCH 31, 2006 AND 2005 (UNAUDITED)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial information included herein is unaudited. The interim consolidated financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, considered necessary for a fair presentation of the Company's consolidated financial position and results of operations for the periods presented. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes presented in the Company's Form 10-KSB for the year ended December 31, 2005. Interim operating results are not necessarily indicative of operating results expected for the entire year.

Description of business

The Company is a manufacturer and assembler of sensors and micro systems, and its products include thin film sensors, thin film pressure sensors and micro-machined pressure sensors, and micro systems that may include sensors, signal conditioning circuits, LCD display, computer interface and molded housing

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specifically designed to the customers needs.

Going concern

The Company incurred a net loss of \$523,284 and a negative cash flow from operations of \$408,443 for three months ended March 31, 2006, and had a working capital deficiency of \$2,231,972 and a stockholders' deficiency of \$2,028,542 at March 31, 2006. These matters raise substantial doubt about its ability to continue as a going concern. Without realization of additional capital, it would be unlikely for the Company to continue as a going concern. Management believes that actions are presently being taken to revise the Company's operating and financial requirements in order to improve the Company's financial position and operating results. However, given the levels of its cash resources and working capital deficiency at March 31, 2006, management believes cash to be generated by operations will not be sufficient to meet anticipated cash requirements for operations, working capital, and capital expenditures during 2006.

Principles of consolidation

The consolidated financial statements for the three months ended March 31, 2006 and 2005 include the accounts and operations of Sensor Systems Solutions Inc. and its wholly-owned subsidiary. Intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Actual results could differ from those estimates.

Stock-based compensation

The Company adopted SFAS No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R), which revises SFAS No. 123 in the first quarter of 2006. SFAS 123R also supersedes APB No. 25 and amends SFAS No. 95, "Statement of Cash Flows". In general, the accounting required by SFAS 123R is similar to that of SFAS No. 123. However, SFAS No. 123 gave companies a choice to either recognize the fair value of stock options in their income statements or disclose the pro forma income statement effect of the fair value of stock options in the notes to the financial statements. SFAS 123R eliminated that choice and requires the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, be recognized in the income statement, generally over the option vesting period.

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SENSOR SYSTEMS SOLUTIONS, INC.
CONDENSED NOTES TO FINANCIAL STATEMENTS
FOR THREE MONTHS ENDED MARCH 31, 2006 AND 2005 (UNAUDITED)

Had compensation cost for all stock option grants been determined based on their fair value at the grant dates in the preceding years, consistent with the method prescribed by SFAS 148 and SFAS 123, the Company's net loss and loss per share would have been adjusted to the pro forma amounts indicated below:

Three months ended
March 31, 2005

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| | |
|---|-------------|
| Net loss | \$(427,935) |
| Add: Stock-based expense included in net loss | 11,942 |
| Deduct: Fair value based stock-based expense | (14,720) |

| | |
|--------------------|-------------------------------|
| Pro forma net loss | ----- \$(430,713) ===== |
|--------------------|-------------------------------|

Basic and diluted earnings per share:

| | |
|------------------------------|----------|
| As reported | \$ (.01) |
| Pro forma under SFAS No. 123 | \$ (.01) |

Earnings (loss) per share

Basic earnings (loss) per common share (EPS) are based on the weighted average number of common shares outstanding during each period. Diluted earnings per common share are based on shares outstanding (computed as under basic EPS) and potentially dilutive common shares. As of March 31, 2006 and 2005, the Company had granted stock options for 1,480,000 and 96,500 shares of common stock, respectively, that are potentially dilutive common shares but are not included in the computation of loss per share because their effect would be anti-dilutive. As of March 31, 2006 and 2005, the Company had granted warrants for 9,477,021 and 8,190,155 shares of common stock, respectively, that are potentially dilutive common shares but are not included in the computation of loss per share because their effect would be anti-dilutive.

Recent Accounting Pronouncements

During the first quarter of 2006, the Company adopted Statement of Financial Accounting Standards No. 151, "Inventory Costs". This Statement amends the guidance in ARB No. 43 Chapter 4 Inventory Pricing, to require items such as idle facility costs, excessive spoilage, double freight and rehandling costs to be expensed in the current period, regardless if they are abnormal amounts or not. The adoption of SFAS No. 151 did not have a material impact on our financial condition, results of operations, or cash flows.

NOTE 2 INVENTORY

Inventory consists of the following at:

| | March 31, 2006 (Unaudited) | December 31, 2005 |
|----------------|-------------------------------|----------------------|
| | ----- | ----- |
| Raw materials | \$158,443 | \$204,748 |
| Finished goods | 95,684 | 97,423 |
| | ----- | ----- |
| | \$254,127 | \$302,171 |
| | ===== | ===== |

NOTE 3 NOTES PAYABLE

Notes payable consist of the following at March 31, 2006 and December 31, 2005:

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| | March 31, 2006 (Unaudited) |
|--|----------------------------------|
| | ----- |
| Two lines of credit, unsecured, interest payable monthly at 10.75% and 11.5% per annum, due on demand. | \$ 92,983 |
| Note payable, unsecured, converted to three-year note in 2006 with monthly principal payments of \$1,112 plus interest at 1% over prime (currently a total of 8.5%). | 36,664 |
| Note payable, unsecured, interest payable monthly at 10% per annum, payable as a percentage of any future private or public stock offerings. | 90,000 |
| Four notes payable, secured by all assets of the Company, interest at 8% per annum, payable at various maturities through May 30, 2006. One note for \$200,000 was due February 21, 2006 and was converted into a note due August 21, 2006. Two notes for \$64,800 and \$32,400 were due on April 18, 2006 and April 20, 2006, respectively. The Company is currently negotiating an extension of these notes. The fourth note, for \$49,707, is due May 30, 2006. At maturity, the notes are convertible at the holder's option at a conversion price equal to 70% of the weighted average price of the common stock for the 30 trading days immediately preceding the conversion date. In addition, each note has warrants attached that, once the note is converted into stock, allow the holder to purchase stock at 85% of the weighted average price of the common stock for the 30 trading days immediately preceding the conversion date. The aggregate intrinsic value of the beneficial conversion feature of these notes and warrants, valued at \$329,679, has been recorded as loan discount costs and is being amortized over the life of the respective note as additional interest cost. | 346,907 |
| Note payable, secured by all assets of the Company, interest at 10% per annum, payable on December 23, 2006. The note is convertible, with some limitations, at the holder's option at a conversion price equal to the lesser of \$0.35 or 90% of the lowest volume weighted average price of the common stock for the 15 trading days immediately preceding the conversion date. In addition, the note has detachable warrants that allow the holder to buy 600,000 shares of common stock at \$0.2878 per share and another 600,000 shares at \$0.35 per share. | 800,000 |
| Note payable, secured by all assets of the Company, interest at 10% per annum, payable on February 14, 2007. The note is convertible, with some limitations, at the holder's option at a conversion price equal to the lesser of \$0.35 or 90% of the lowest volume weighted average price of the common stock for the 15 trading days immediately preceding the conversion date. | 200,000 |
| Less, remaining debt discount | (311,334) |
| | ----- |
| | 1,255,220 |
| Less, non-current portion of notes | (26,656) |
| | ----- |
| | \$1,228,564 |
| | ===== |

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once the note is converted into stock, allow the holder to purchase stock at 85% of the weighted average price of the common stock for the 30 trading days immediately preceding the conversion date. The intrinsic value of the Beneficial conversion feature of the note and warrants, valued at \$32,143, has been recorded as loan discount costs and is being amortized over the life of the note as additional interest cost. This note and accrued interest was converted into 342,000 shares of common stock at maturity.

Less, remaining debt discount

(240)

\$ 376,025
=====

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SENSOR SYSTEMS SOLUTIONS, INC.
CONDENSED NOTES TO FINANCIAL STATEMENTS
FOR THREE MONTHS ENDED MARCH 31, 2006 AND 2005 (UNAUDITED)

NOTE 5 INVESTMENT IN AFFILIATED ENTITIES

Universal Sensors, Inc.

In April 2005, the Company, China Automotive Systems, Inc. (CAAS) and Shanghai Hongxi Investment Inc. (HX) formed Universal Sensors, Inc. (USI), a joint venture in the People's Republic of China to develop, produce and market sensor and related electronic products. The ownership percentages of USI are 30%, 60% and 10% to the Company, CAAS and HX, respectively. CAAS and HX will contribute cash, land and building and the Company will contribute technology. As there was no cash contributed by the Company and the technology it will contribute is not recorded as an asset on the Company's books, the Company's investment in USI is recorded at zero. USI is in a start-up mode and had not begun operations as of March 31, 2006. USI has incurred cumulative losses at March 31, 2006 of approximately \$347,000, including \$115,000 for the three months then ended. The Company has not recorded any loss from USI since its investment is zero. The Company will not record any income in the future until such time as USI is cumulatively profitable. The company has no liability for future cash payments to USI if necessary to fund its operations or pay its debts.

During the three months ended March 31, 2006, the Company sold some of its tooling equipment to USI. The equipment had an original cost and remaining book value of approximately \$118,000 and \$62,000, respectively. The Company recorded a gain on the sale of \$16,905.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

CAUTIONARY STATEMENT

STATEMENTS IN THIS REPORT ON FORM 10-QSB THAT ARE FORWARD-LOOKING ARE BASED ON CURRENT EXPECTATIONS. ACTUAL RESULTS MAY DIFFER MATERIALLY. FORWARD-LOOKING STATEMENTS INVOLVE NUMEROUS RISKS AND UNCERTAINTIES INCLUDING, BUT NOT LIMITED TO, THE POSSIBILITY THAT THE DEMAND FOR OUR PRODUCTS MAY DECLINE AS A RESULT OF POSSIBLE CHANGES IN GENERAL AND INDUSTRY SPECIFIC ECONOMIC CONDITIONS, THE EFFECTS OF COMPETITIVE PRICING AND SUCH OTHER RISKS AND UNCERTAINTIES AS ARE

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DESCRIBED IN THIS REPORT ON FORM 10-QSB AND OTHER DOCUMENTS PREVIOUSLY FILED OR HEREAFTER FILED BY US FROM TIME TO TIME WITH THE SECURITIES AND EXCHANGE COMMISSION. ALL FORWARD-LOOKING STATEMENTS SPEAK ONLY AS OF THE DATE MADE, AND WE UNDERTAKE NO OBLIGATION TO UPDATE THESE FORWARD-LOOKING STATEMENTS .

The following discussion and analysis should be read in conjunction with the consolidated financial statements and the notes thereto, included as part of this Quarterly Report.

OVERVIEW

Sensor System Solutions, Inc. (3S) was founded by an engineering management team with over 50 years of Micro-electro-mechanical-systems or "MEMS" transducer experience. Its objective is to provide high quality sensors and transducers at an economical price by employing innovative designs and creative manufacturing methods. 3S offers a variety of digital pressure gauges, pressure transducers, pressure sensors, force beams, load cells, intelligent sensor interface electronics, intelligent embedded control systems, and wireless communication network interfaces.

3S has 17 employees in the United States, and utilizes a network of independent contractors and consultants throughout the United States and Asia. 3S produces or supplies a family of nearly 30 distinctive products. 3S formed a joint venture in China with China Automotive Systems, Inc. (NASDAQ: CAAS) in April of 2005, targeting its automotive sensor market. 3S is transitioning to move its production line in Taiwan to this joint venture. 3S is a supplier of thin-film and micro-machined force and pressure sensors to the medical, chemical, oil, and gas industries. 3S believes that its technology will enable it to become a global supplier of advanced MEMS/Microelectronic products in a myriad of developing markets. 3S's strategic plan is to focus on developing custom MEMS pressure sensor devices and forming strategic partnerships where its strategic partners dominate the sales channels in industries accepting MEMS sensor applications.

3S commenced operations as a private company in September of 1996. 3S is headquartered in Irvine, California where 3S occupies a 25,000 square foot facility fully equipped with fabrication capability.

STRATEGIC PLAN

We plan to grow our business in four areas.

- o INCREASE THE REVENUE OF OUR EXISTING SENSOR COMPONENT BUSINESS. Once finalized, the majority of our sensor component manufacturing will be moved to our joint venture in China to help reduce the cost of our products. We will invest to increase our production capacity and will qualify offshore suppliers to meet the increasing demands. Substantial efforts will be invested in sales and marketing in order to expand our customer base and to secure additional OEM projects.
- o DEVELOP SENSOR SOLUTION BUSINESS. By leveraging the advances in technology and the large industry-wide investments in wireless and telecommunication in the last decade, we can now offer total sensor solutions at a very affordable price. These sensor solutions are modules containing sensing elements, signal conditioning circuitry, software for calibration and interface, and capability of wireless communication and/or networking. They will provide information continuously to decision makers in all phases of business operation.
- o PENETRATE THE AUTOMOTIVE SENSOR MARKET IN CHINA AND INDIA. By leveraging the marketing channel of USI, our joint venture partner, and X-Lab Global, a leading technology advisory and strategic consulting firm, we will have

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access to the automotive market in China and India immediately. We plan to use the next two years to build up our production capacity, product offerings and technical team there. We expect to import automotive sensors produced by our joint venture to North America and Europe around 2008.

- o STRATEGIC ACQUISITION: Being a public company gives us a supplemental tool to grow our business through acquisition in addition to internal growth. We will actively seek equity or debt funding to bring in the necessary resources to execute this plan.

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RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2006 AND 2005

REVENUES

We generated revenues of \$530,098 for the three months ended March 31, 2006, which was \$325,083 or a 159% increase from \$205,015 for the three months ended March 31, 2005. The increase is the result of the hiring of a full-time sales manager, the addition of new sales representatives and the introduction of new products.

GROSS PROFIT

Gross profit for the three months ended March 31, 2006, was \$197,105 or 37.2% of revenues, compared to \$57,741 or 28.2% for the three months ended March 31, 2005. The \$139,364 increase in gross profit was generated by a decrease in cost of sales percentage, which was the result of increased productivity and management's efforts to reduce operating expense, and production tooling improvement.

TOTAL OPERATING EXPENSES

Operating expenses

Operating expenses increased to \$544,817 for the three months ended March 31, 2006 compared to \$330,555 for the three months ended March 31, 2005. The expenses increased \$214,262, primarily as a result of an increase in interest expense, rent, additional investment in R&D personnel and development, and professional fees for a public company.

Amortization of discount on notes payable

Amortization of discount on notes payable decreased to \$132,448 for the three months ended March 31, 2006 compared to \$155,121 for the three months ended March 31, 2005. The expense decreased \$22,673, or 15%, primarily due to the lack of the Sino-America convertible loan in 2006.

Stock-based compensation costs

During the three months ended March 31, 2006, the Company recorded \$22,635 in stock-based compensation costs for options issued to employees during the quarter. Another \$37,394 was recorded for compensatory stock issued to non-employees for services rendered. There were no stock-based compensation costs in the three months ended March 31, 2005.

NET LOSS

Net loss increased to (\$523,284) for the three months ended March 31, 2006

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compared to (\$427,935) for the three months ended March 31, 2005. The \$95,349 increase in net loss is primarily due to the increase in operating expenses exceeding the increase in gross profit and is partially offset by the \$16,905 gain on sale of equipment to related party.

FINANCIAL CONDITION, LIQUIDITY, CAPITAL RESOURCES

GOING CONCERN

The Company incurred a net loss of \$523,284 and a negative cash flow from operations of \$408,443 for three months ended March 31, 2006, and had a working capital deficiency of \$2,231,972 and a stockholders' deficiency of \$2,028,542 at March 31, 2006. These matters raise substantial doubt about its ability to continue as a going concern.

We have relied primarily on cash flow from operations, bank loans, and advances and investments from our shareholders for our capital requirements since inception. The company received an additional \$200,000 on a convertible loan from an outside source in February 2006, bringing the total owed to that lender to \$1 million. This allowed the company to pay off some of the debt and continue its operation. Current cash on hand will allow the company to continue its operation for only a short period of time.

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At March 31, 2006, cash was \$38,038 as compared to \$172,732 at December 31, 2005. The decrease is due to the negative cash flow from operations, primarily due to funding an increase in accounts receivable of \$186,411 created by the increase in sales. The cash flows from investing and financing activities totaling \$273,749 was not enough to fund the \$408,443 in net cash used in operations. We have a substantial working capital deficit. We require \$3,000,000 to continue operations for the next three years. We are in the process of raising capital in the form of equity and/or debt. However, there is no guarantee that we will raise sufficient funds to execute our business plan. To the extent we are unable to raise sufficient funds, our business plan will be required to be substantially modified, its operations curtailed or protection under bankruptcy/ reorganization laws sought.

We are addressing our liquidity requirements by the following actions: Continue our programs for selling products; continue to seek investment capital through the public markets. However, there is no guarantee that these strategies will enable us to meet our obligations for the foreseeable future.

COMMITMENTS AND CONTINGENCIES

We have the following material contractual obligations and capital expenditure commitments:

The Company leases certain equipment under two capital leases with monthly payments of \$360 and \$701, respectively, including interest at 12.75% per annum.

Future minimum annual rental payments for capitalized leases are as follows:

| As of March 31, 2006 | Amount |
|----------------------|----------|
| 2006 (nine months) | \$ 9,549 |
| 2007 | 12,732 |
| 2008 | 12,732 |
| 2009 | 3,903 |

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| | |
|---|-------------------|
| Amount representing interest | 38,916 (6,832) |
| | ----- |
| Present value of minimum lease payments | 32,084 |
| Less: Current portion | (9,163) |
| | ----- |
| | \$ 22,921 |
| | ===== |

The Company leases its office and facility through July 31, 2007 under a long-term operating lease agreement. Under terms of the lease, the Company pays the cost of repairs and maintenance.

Future minimum lease commitments for the Company's share under this lease at March 31, 2006 are as follows:

| | | |
|--------------------|----|---------|
| 2006 (nine months) | \$ | 189,625 |
| 2007 | | 151,095 |
| | | ----- |
| | \$ | 340,720 |
| | | ===== |

INFLATION AND CHANGING PRICES

We do not foresee any adverse effects on our earnings as a result of inflation or changing prices.

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CRITICAL ACCOUNTING POLICIES

REVENUE RECOGNITION

The Company recognizes revenue when risk of loss and title to the product is transferred to the customer, which occurs at shipment.

STOCK - BASED COMPENSATION

The Company adopted SFAS No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R), which revises SFAS No. 123 in the first quarter of 2006. SFAS 123R also supersedes APB No. 25 and amends SFAS No. 95, "Statement of Cash Flows". In general, the accounting required by SFAS 123R is similar to that of SFAS No. 123. However, SFAS No. 123 gave companies a choice to either recognize the fair value of stock options in their income statements or disclose the pro forma income statement effect of the fair value of stock options in the notes to the financial statements. SFAS 123R eliminates that choice and requires the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, be recognized in the income statement, generally over the option vesting period.

INVENTORIES

Inventories are stated at the lower of cost (first-in, first-out method) or market.

RECENT ACCOUNTING PRONOUNCEMENTS

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In May 2005, the FASB issued Statement No. 154 ("SFAS 154") "Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3." SFAS 154 changes the requirements for the accounting for and reporting of a change in accounting principle. APB Opinion 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. SFAS 154 requires retrospective application to prior periods' financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects of the cumulative effect of the change. In the event of such impracticability, SFAS 154 provides for other means of application. In the event the Company changes accounting principles, it will evaluate the impact of SFAS 154.

RISKS RELATED TO OUR BUSINESS

WE HAVE HAD NEGATIVE CASH FLOWS FROM OPERATIONS. OUR BUSINESS OPERATIONS MAY FAIL IF OUR ACTUAL CASH REQUIREMENTS EXCEED OUR ESTIMATES, AND WE ARE NOT ABLE TO OBTAIN FURTHER FINANCING.

Our company has had negative cash flows from operations. To date, we have incurred significant expenses in product development and administration in order to ready our products for market. Our business plan calls for additional significant expenses necessary to bring our products to market. We believe we do not have sufficient funds to satisfy our short-term cash requirements. There is no assurance that actual cash requirements will not exceed our estimates, in which case we will require additional financing to bring our products into commercial operation, finance working capital and pay for operating expenses and capital requirements until we achieve a positive cash flow. In particular, additional capital may be required in the event that:

- o we incur unexpected costs in completing the development of our technology or encounter any unexpected technical or other difficulties;
- o we incur delays and additional expenses as a result of technology failure;
- o we are unable to create a substantial market for our product and services; or
- o we incur any significant unanticipated expenses.

We may not be able to obtain additional equity or debt financing on acceptable terms if and when we need it. Even if financing is available it may not be available on terms that are favorable to us or in sufficient amounts to satisfy our requirements. If we require, but are unable to obtain, additional financing in the future, we may be unable to implement our business plan and our growth strategies, respond to changing business or economic conditions, withstand adverse operating results, and compete effectively. More importantly, if we are unable to raise further financing when required, our continued operations may have to be scaled down or even ceased and our ability to generate revenues would be negatively affected.

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A DECLINE IN THE PRICE OF OUR COMMON STOCK COULD AFFECT OUR ABILITY TO RAISE FURTHER WORKING CAPITAL AND ADVERSELY IMPACT OUR OPERATIONS.

A prolonged decline in the price of our common stock could result in a reduction in the liquidity of our common stock and a reduction in our ability to raise capital. Because our operations have been primarily financed through the sale of equity securities, a decline in the price of our common stock could be especially detrimental to our liquidity and our continued operations. Any

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reduction in our ability to raise equity capital in the future would force us to reallocate funds from other planned uses and would have a significant negative effect on our business plans and operations, including our ability to develop new products and continue our current operations. If the stock price declines, there can be no assurance that we can raise additional capital or generate funds from operations sufficient to meet our obligations.

IF WE ISSUE ADDITIONAL SHARES IN THE FUTURE THIS MAY RESULT IN DILUTION TO OUR EXISTING STOCKHOLDERS.

Our Amended Certificate of Incorporation authorizes the issuance of 200,000,000 shares of common stock. Our board of directors has the authority to issue additional shares up to the authorized capital stated in the certificate of incorporation. Our board of directors may choose to issue some or all of such shares to acquire one or more businesses or to provide additional financing in the future. The issuance of any such shares may result in a reduction of the book value or market price of the outstanding shares of our common stock. It will also cause a reduction in the proportionate ownership and voting power of all other stockholders. Further, any such issuance may result in a change of control of our corporation.

WE HAVE A HISTORY OF LOSSES AND NEGATIVE CASH FLOWS, WHICH IS LIKELY TO CONTINUE UNLESS OUR PRODUCTS GAIN SUFFICIENT MARKET ACCEPTANCE TO GENERATE A COMMERCIALY VIABLE LEVEL OF SALES.

From inception through March 31, 2006, we have incurred aggregate net losses. There is no assurance that we will operate profitably or will generate positive cash flow in the future. In addition, our operating results in the future may be subject to significant fluctuations due to many factors not within our control, such as market acceptance of our products, the unpredictability of when customers will order products, the size of customers' orders, the demand for our products, and the level of competition and general economic conditions.

Although we anticipate that we will be able to increase revenues during the next 9 months, we also expect an increase in development and operating costs. Consequently, we expect to incur operating losses and net cash outflow unless and until our existing products, and/or any new products that we may develop, gain market acceptance sufficient to generate a commercially viable and sustainable level of sales.

UNLESS WE CAN ESTABLISH SIGNIFICANT SALES OF OUR CURRENT PRODUCTS, OUR POTENTIAL REVENUES MAY BE SIGNIFICANTLY REDUCED.

We expect that a substantial portion, if not all, of our future revenue will be derived from the sale of our sensor products. We expect that these product offerings and their extensions and derivatives will account for a majority, if not all, of our revenue for the foreseeable future. The successful introduction and broad market acceptance of our sensor products - as well as the development, introduction and market acceptance of any future enhancements - are, therefore, critical to our future success and our ability to generate revenues. Unfortunately, there can be no assurance that we will be successful in marketing our current product offerings, or any new product offerings, applications or enhancements. Failure to achieve broad market acceptance of our sensor products, as a result of competition, technological change, or otherwise, would significantly harm our business.

WE COULD LOSE OUR COMPETITIVE ADVANTAGES IF WE ARE NOT ABLE TO PROTECT ANY PROPRIETARY TECHNOLOGY AND INTELLECTUAL PROPERTY RIGHTS AGAINST INFRINGEMENT, AND ANY RELATED LITIGATION COULD BE TIME-CONSUMING AND COSTLY.

Our success and ability to compete depends to a significant degree on our proprietary technology incorporated in our products. We have taken limited

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action to protect our proprietary technology and proprietary computer software. If any of our competitors copies or otherwise gains access to our proprietary technology or software or develops similar technologies independently, we would not be able to compete as effectively.

Further, the laws of foreign countries may provide inadequate protection of such intellectual property rights. We may need to bring legal claims to enforce or protect such intellectual property rights. Any litigation, whether successful or unsuccessful, could result in substantial costs and diversions of resources. In addition, notwithstanding any rights we have secured in our intellectual property, other persons may bring claims against us that we have infringed on their intellectual property rights, including claims based upon the content we license from third parties or claims that our intellectual property right interests are not valid. Any claims against us, with or without merit, could be time consuming and costly to defend or litigate, divert our attention and resources, result in the loss of goodwill associated with our service marks or require us to make changes to our website or other of our technologies.

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OUR PRODUCTS MAY BECOME OBSOLETE AND UNMARKETABLE IF WE ARE UNABLE TO RESPOND ADEQUATELY TO RAPIDLY CHANGING TECHNOLOGY AND CUSTOMER DEMANDS.

Our industry is characterized by rapid changes in technology and customer demands. As a result, our products may quickly become obsolete and unmarketable. Our future success will depend on our ability to adapt to technological advances, anticipate customer demands, develop new products and enhance our current products on a timely and cost-effective basis. Further, our products must remain competitive with those of other companies with substantially greater resources. We may experience technical or other difficulties that could delay or prevent the development, introduction or marketing of new products or enhanced versions of existing products. Also, we may not be able to adapt new or enhanced products to emerging industry standards, and our new products may not be favorably received.

IF WE FAIL TO EFFECTIVELY MANAGE OUR GROWTH OUR FUTURE BUSINESS RESULTS COULD BE HARMED AND OUR MANAGERIAL AND OPERATIONAL RESOURCES MAY BE STRAINED .

As we proceed with the commercialization of our products, we expect to experience significant and rapid growth in the scope and complexity of our business. We will need to add staff to market our products, manage operations, handle sales and marketing efforts and perform finance and accounting functions. We will be required to hire a broad range of additional personnel in order to successfully advance our operations. This growth is likely to place a strain on our management and operational resources. The failure to develop and implement effective systems, or to hire and retain sufficient personnel for the performance of all of the functions necessary to effectively service and manage our potential business, or the failure to manage growth effectively, could have a materially adverse effect on our business and financial condition.

OFF BALANCE SHEET ARRANGMENTS

There are no Off-Balance Sheet Arrangements to report.

ITEM 3. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures.

Our management evaluated, with the participation of our Chief Executive and Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-QSB .

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Based on this evaluation, our Chief Executive and Financial Officer has concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)) are inadequate to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms. We are developing a plan to ensure that all information will be recorded, processed, summarized and reported on a timely basis. This plan is dependent, in part, upon reallocation of responsibilities among various personnel, possibly hiring additional personnel and additional funding. It should also be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

(b) Changes in Internal Controls.

During the period covered by the Quarterly Report on Form 10-QSB, there were no significant changes in our internal controls over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

None.

ITEM 2. CHANGES IN SECURITIES AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES.

On February 14, 2006, the Company issued a note payable for \$200,000, secured by all assets of the Company, interest at 10% per annum, payable on February 14, 2007. The note is convertible, with some limitations, at the holder's option at a conversion price equal to the lesser of \$0.35 or 90% of the lowest volume weighted average price of the common stock for the 15 trading days immediately preceding the conversion date.

On February 22, 2006, the Company issued a note payable for \$200,000, secured by all assets of the Company, interest at 8% per annum, payable on August 21, 2006. The note is convertible at the holder's option at a conversion price equal to the 75% of the average closing bid price of the common stock for the month of February 2006. The note has 3-year warrants attached that allow the holder, if he converts, to purchase an identical number of shares at 85% of the average bid price of the common stock for the 30 trading days preceding exercise.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

The \$190,665 promissory note due to Tina Young matured on December 31, 2004. The Company is currently negotiating a settlement.

The \$110,000 convertible loan due to Tina Young matured on March 16, 2005. The Company is currently negotiating a settlement.

A \$64,800 convertible loan matured on April 18, 2006. The Company is currently negotiating an extension of the note.

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A \$32,400 convertible loan matured on April 20, 2006. The Company is currently negotiating an extension of the note.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS

31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SENSOR SYSTEM SOLUTIONS, INC.

Dated: May 25, 2006

/s/ Michael Young

Name: Michael Young
Title: Chief Executive Officer and
Principal
Accounting Officer

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