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TAITRON COMPONENTS INC  
Form 10QSB  
August 14, 2006

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

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended June 30, 2006

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from \_\_\_\_\_ to \_\_\_\_\_

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)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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

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

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

Class	Outstanding on July 31, 2006
-----	-----
Class A common stock, \$.001 par value	4,716,811
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 Sheet  
(Dollars in Thousands)

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Assets

Current assets:

Cash and cash equivalents  
Trade accounts receivable, net  
Inventory, net  
Prepaid expenses and other current assets

Total current assets

Property and equipment, net  
Other assets

Total assets

Liabilities and Shareholders' Equity

Current liabilities:

Trade accounts payable  
Accrued liabilities and other

Total current liabilities

Total liabilities

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 4,716,811 shares  
Class B common stock, \$.001 par value. Authorized, issued and outstanding  
762,612 shares  
Additional paid-in capital  
Accumulated other comprehensive loss, net of tax  
Retained earnings

Total shareholders' equity

Total liabilities and shareholders' equity

See accompanying notes to condensed consolidated financial statements.

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TAITRON COMPONENTS INCORPORATED

Condensed Consolidated Statements of Operations  
(Dollars in Thousands, except per share amounts)

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	Three months ended June 30,		S
	2006	2005	2
	----- (Unaudited)	----- (Unaudited)	(Una
Net sales	\$ 2,996	\$ 2,202	\$
Cost of goods sold	2,133	1,616	
	-----	-----	
Gross profit	863	586	
Selling, general and administrative expenses	704	628	
	-----	-----	
Income (loss) from operations	159	(42)	
Interest income (expense), net	22	(5)	
Other (expense) income, net	(19)	39	
	-----	-----	
Income (loss) before income taxes	162	(8)	
Income tax provision	-	-	
	-----	-----	
Net income (loss)	\$ 162	\$ (8)	\$
	=====	=====	=====
Other comprehensive income (loss):			
Foreign currency translation adjustment	11	(1)	
	-----	-----	
Comprehensive income (loss)	\$ 173	\$ (9)	\$
	=====	=====	=====
Income (loss) per share			
Basic	\$ .03	\$ (.00)	\$
	=====	=====	=====
Diluted	\$ .03	\$ (.00)	\$
	=====	=====	=====
Weighted average common shares outstanding			
Basic	5,479,423	5,462,479	5,
	=====	=====	=====
Diluted	5,918,423	5,462,479	5,
	=====	=====	=====

See accompanying notes to condensed consolidated financial statements.

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	Six months en
	2006
	----- (Unaudited)
Cash flows from operating activities:	
Net loss	\$    --
	-----
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation and amortization	106
Provision for sales returns and doubtful accounts	15
Stock-based compensation	10
Changes in assets and liabilities:	
Trade accounts receivable	(813)
Inventory, net	582
Prepaid expenses and other current assets	31
Other assets	(41)
Trade accounts payable	311
Accrued liabilities and other	(21)
	-----
Total adjustments	180
	-----
Net cash provided by operating activities	180
	-----
Cash flows from investing activities:	
Acquisitions of property and equipment	(31)
	-----
Net cash used in investing activities	(31)
	-----
Cash flows from financing activities:	
Payments on notes payable	--
Proceeds from exercise of stock options and issuance of stock	24
	-----
Net cash provided by (used in) financing activities	24
	-----
Impact of exchange rate changes on cash	23
	-----
Net increase in cash and cash equivalents	196
Cash and cash equivalents, beginning of period	1,962
	-----
Cash and cash equivalents, end of period	\$ 2,158
	=====
Supplemental disclosure of cash flow information:	
Cash paid for interest	\$    --
	=====
Cash paid for income taxes	\$    13
	=====

See accompanying notes to condensed consolidated financial statements.

TAITRON COMPONENTS INCORPORATED

Notes to Condensed Consolidated Financial Statements

June 30, 2006

(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, 2005, 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 60% majority-owned subsidiary, Taitron Components Mexico SA de CV. 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 June 30, 2006 and 2005 were \$81,000 and \$44,000, respectively, and for the six months ended June 30, 2006 and 2005 aggregated \$96,000 and \$61,000, 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 June 30, 2006 aggregated \$70,000.

Inventory

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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 \$1,024,000 at June 30, 2006.

### 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

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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.

### Per Share Data

Basic earnings per share data are based upon the weighted average number of common shares outstanding. Diluted earnings per share data are based upon the weighted average number of common shares outstanding, plus the number of common shares potentially issuable for dilutive securities such as stock options and warrants. The weighted average number of common shares outstanding for each of the three and six month periods ended June 30, 2006 and 2005 is set forth in the following table:

	Three months ended		S
	June 30		
	2006	2005	
Basic weighted average shares outstanding	5,479,423	5,462,479	5,475
Potentially dilutive stock options	439,000	603,000	473
Anti-dilutive stock options due to net loss in period	--	(603,000)	
Diluted weighted average shares outstanding	5,918,423	5,462,479	5,948

### 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

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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.

### Stock-Based Compensation

In March 1995, the Company established the 1995 Stock Incentive Plan (the "1995 Plan") that expired in March 2005. The 1995 Plan provided for the issuance of an aggregate 1,080,000 incentive stock options, nonstatutory options or stock appreciation rights (SAR's) to directors, officers and other employees of the Company. Under the 1995 Plan, incentive stock options were granted at prices equal to at least the fair market value of the Company's Class A common stock at the date of grant. Nonstatutory options and stock appreciation rights were granted at prices equal to at least 85% and 100%, respectively, of the fair market value of the Company's Class A common stock at the date of grant. Outstanding options and rights vest in three equal annual installments beginning one year from the date of grant and are subject to termination provisions as defined in the 1995 Plan. The 1995 Plan also provided for automatic grants of nonstatutory options to purchase 5,000 shares of Class A common stock to all members of the committee administering the 1995 Plan, upon their initial election to the committee and each year thereafter. The exercise prices of these options are equal to the fair market value of the Company's Class A common stock at the date of grant. The fair value of options is the estimated present value at grant date using the Black-Scholes option-pricing model with the following weighted average assumptions used for 2005: dividend yield of 0%; expected volatility of 35%; a risk free interest rate of approximately 5% and an expected holding period of five years.

In June 2006, the Company's shareholders approved the 2005 Stock Incentive Plan (the "2005 Plan"), which authorizes the issuance of up to 1,000,000 shares pursuant to options or awards granted under the plan. No shares have yet been granted under the 2005 Plan, while it's pending approval by state regulators.

Effective January 1, 2006, the Company adopted SFAS No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R). SFAS 123R requires that the Company account for all stock-based compensation using a fair-value method and recognize the fair value of each award as an expense over the service period. For the year ended December 31, 2005 and earlier years, the Company accounted for employee stock-based compensation

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using the intrinsic value method of APB Opinion No. 25 and followed the disclosure requirements of SFAS No. 123, as amended by SFAS 148.

The Company elected to adopt SFAS 123R using the "modified prospective application." Under that method, compensation expense includes the fair value of new awards, modified awards and any unvested awards outstanding at January 1, 2006. However, the consolidated financial statements for periods prior to the adoption of SFAS 123R have not been restated to reflect the fair value method of accounting for stock-based compensation, but rather disclosed the cost in accordance with APB 25.

The following table illustrates the effect on net loss and net loss per share as if compensation expense for all awards of stock-based employee compensation had been determined under the fair value-based method prescribed by SFAS 123 for periods prior to the adoption of SFAS 123R:

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	Three months ended June 30, 2005 -----	Six months ended June 30, 2005 -----
Net loss, as reported	\$ (8,000)	\$ (137,000)
Net loss, pro forma	\$ (2,000)	\$ (125,000)
Diluted loss, as reported	--	\$ (0.03)
Diluted loss, pro forma	--	\$ (0.02)

Stock option activity during the periods indicated is as follows:

	Number of Shares	Weighted Average Exercise Price
Balance at December 31, 2005	526,166	\$ 1.78
Exercised	(16,666)	\$ 1.41
	-----	
Balance at June 30, 2006 (Unaudited)	509,500	\$ 1.80
	=====	

The weighted average fair value of options granted in the three months and six months periods ended June 30, 2006 and 2005 was \$0, as there were no options granted during these periods.

At June 30, 2006, the range of individual weighted average exercise prices was \$1.29 to \$2.17. The remaining contractual life of outstanding options is 90 days after termination of employment of option holder.

At June 30, 2006, the approximate number of options exercisable was 466,000 and the weighted average exercise prices of those exercisable options were \$1.80.

### Note 3 - Commitments and Contingencies

Effective July 1, 2006, the European Union ("EU") began restricting the distribution of products within the EU containing certain substances, including lead. At the present time, much of the Company's inventory contains substances prohibited by the RoHS directive and management believes it is likely that the Company 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 the Company's inventory may become obsolete and unsaleable and, as a result, have to be written off. However, we believe the demand from our customers requiring only the RoHS compliant products has already been experienced during the periods leading up to the directive's restriction date.

On July 10 2006, we entered into commitments for purchasing approximately 4,500 square feet of office space in Shanghai, China for \$1,230,000. The investment will be used as rental property for lease to others and for our project design and engineering center.

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

The following discussion should be read in conjunction with the condensed



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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, 2005. 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 June 30, 2006 and 2005 were \$81,000 and \$44,000, respectively, and for the six months ended June 30, 2006 and 2005 aggregated \$96,000 and \$61,000, respectively. The allowance for sales returns and doubtful accounts at June 30, 2006 aggregated \$70,000.

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 \$16,099,000 at June 30, 2006, which is presented net of valuation allowances of \$1,024,000. We evaluate inventories to identify excess, high-cost, slow-moving or other factors rendering inventories as unmarketable at normal profit margins. 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

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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

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such obsolete inventory. However, we believe the demand from our customers requiring only the RoHS compliant products has already been experienced during the periods leading up to the directive's restriction date.

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 against our net deferred tax assets.

### Selected Recent Accounting Policies

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140 ("SFAS 156") which amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities. This statement clarifies when servicing rights should be separately accounted for, requires companies to account for separately recognized servicing rights initially at fair value, and gives companies the option of subsequently accounting for those servicing rights at either fair value or under the amortization method. SFAS 156 is effective for fiscal years beginning after September 15, 2006. We do not believe that adoption of SFAS 156 will have a material impact on our financial statements.

### 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 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 have been refocusing our business strategy beyond the traditional role of electronic components fulfillment to the additional role of engineering and turn-key

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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) solutions for their multi-year turn-key projects. We are beginning to see the results from these additional products 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

Second quarter of 2006 versus Second quarter of 2005.

Net sales in the second quarter of 2006 totaled \$2,996,000 versus \$2,202,000 in the comparable period for 2005, an increase of 36.1% over the same period last year. The sales increase was attributed to growth in our ODM products by \$853,000 comparing the second quarter of 2006 over the same period last year.

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Gross profit for the second quarter of 2006 was \$863,000 versus \$586,000 in the comparable period for 2005, and gross margin percentage of net sales was 28.8% in 2006 versus 26.6% in 2005. The increase was primarily attributed to the impact from our ODM products.

Selling, general and administrative ("SG&A") expenses in the second quarter of 2006 totaled \$704,000 versus \$628,000 in the comparable period for 2005. As a percentage of net sales, SG&A expenses were 23.5% in the second quarter of 2006 compared to 28.5% in the second quarter for 2005. The increase of \$76,000 was primarily attributable to personnel related expenses from our engineering center in China and higher trade commissions to our sales representatives for ODM products.

Interest income, net of interest expense, was \$22,000 for the second quarter of 2006 versus interest expense, net of interest income, of \$5,000 in the comparable period for 2005. The change is due to earning interest on cash investments in 2006 after repaying all debt obligations in 2005.

Income tax provision was \$0 for the second quarter of 2006 and in the comparable period for 2005, as we do not expect significant taxable income for fiscal year 2006.

Net income was \$162,000 for the second quarter of 2006 versus a loss of \$8,000 in the comparable period for 2005, an increase of \$170,000.

Six Months Ended June 30, 2006 versus Six Months Ended June 30, 2005.

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Net sales in the six months ended June 30, 2006 was \$4,985,000 versus \$4,044,000 in the comparable period for 2005, an increase of 23.3% over the same period last year. The sales increase was attributed to growth in our ODM products by \$976,000 comparing the six months ended June 30, 2006 over the same period last year.

Gross profit for the six months ended June 30, 2006 was \$1,343,000 versus \$1,087,000 in the comparable period for 2005, and gross margin percentage of net sales was 26.9% for both periods. The dollar increase was primarily attributed to the impact from our ODM products.

Selling, general and administrative ("SG&A") expenses in the six months ended June 30, 2006 totaled \$1,340,000 versus \$1,246,000 in the comparable period for 2005. As a percentage of net sales, SG&A expenses were 26.9% in the six months ended June 30, 2006 compared to 30.8% in the comparable period for 2005. The increase of \$94,000 was primarily attributable to personnel related expenses from our engineering center in China and higher trade commissions to our sales representatives for ODM products.

Interest income, net of interest expense, was \$37,000 for the six months ended June 30, 2006 versus interest expense, net of interest income, of \$17,000 in the comparable period for 2005. The change is due to earning interest on cash investments in 2006 after repaying all debt obligations in 2005.

Income tax provision was \$4,000 for the six months ended June 30, 2006 versus \$0 in the comparable period for 2005, as we do not expect significant taxable income for fiscal year 2006.

Net income was \$0 for the six months ended June 30, 2006 versus net losses of \$137,000 in the comparable period for 2005, an increase of \$137,000 resulting from the reasons discussed above.

Effective January 1, 2006, we adopted SFAS 123(R) and such had a \$10,000 financial impact to our SG&A for the six months ended June 30, 2006.

### 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 six months ended June 30, 2006 and 2005 are as follows:

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(Dollars in thousands)	Six months ended June 30,	
	2006	2005
	(Unaudited)	(Unaudited)
Operating activities .....	\$ 180	\$ 662
Investing activities .....	(31)	(23)
Financing activities .....	24	(71)

Cash provided by operating activities for the six months ended June 30, 2006 and 2005 was \$180,000 and \$662,000, respectively. The decrease was primarily attributed to the increase of accounts receivable by \$813,000 for the six months ended June 30, 2006 versus the increase of \$282,000 in the comparable

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period for 2005.

Cash used in investing activities for the six months ended June 30, 2006 and 2005 was \$31,000 and \$23,000, respectively, for capital expenditures.

Cash provided by financing activities for the six months ended June 30, 2006 was \$24,000 versus \$71,000 used in, during the comparable period in 2005. The increase was primarily attributed to repayments on notes payable of \$73,000 in the six months ended June 30, 2005.

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 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 short-term commercial loans, asset-based lending on accounts receivables or issue debt or equity securities.

As of the date of this Report, we have the commitment for purchasing approximately 4,500 square feet of office space in Shanghai, China for \$1,230,000. The investment will be used as rental property for lease to others and for our project design and engineering center. 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 quarterly 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. Unregistered Sales of Equity Securities and Use of Proceeds.

There were no issuances or sales of our securities by us during the quarter ended June 30, 2006 that were not registered under the Securities Act.

### Item 3. Defaults Upon Senior Securities.

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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.

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SIGNATURES

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

TAITRON COMPONENTS INCORPORATED

Date: August 14, 2006

By: /s/ Stewart Wang

-----  
Stewart Wang  
Chief Executive Officer, President,  
Chief Financial Officer and Director  
(Principal Executive, Financial and  
Accounting Officer)

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