SENSOR SYSTEM SOLUTIONS INC
Form 10QSB
November 20, 2006

U.S. Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended September 30, 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	98-0204898
(State or other jurisdiction of incorporation or organization)	(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 |X| No |_|

As of November 7, 2006 there were 78,828,002 shares of Common Stock outstanding.

Transitional Small Business Disclosure Format

Yes |_| No |X|

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
As of September 30, 2006 (Unaudited) and December 31, 2005

	September 30, 200 (Unaudited)

ASSETS

CURRENT ASSETS	
Cash	$ 31,417
Accounts receivable	100,441
Accounts receivable, related party	53,628
Inventory	263,865
Prepaids and other current assets	2,588
Total current assets	451,939
Property and equipment, net	119,861
Other assets	104,112
Total assets	$ 675,912

LIABILITIES AND STOCKHOLDERS' DEFICIENCY

CURRENT LIABILITIES	
Accounts payable and accrued expenses	$ 1,555,224
Accounts payable, related party	187,218
Notes payable	1,423,877
Notes payable, related parties	315,853
Current portion of capital lease obligations	9,763
Current portion of deferred rent concession	5,272
Total current liabilities	3,497,207
LONG-TERM LIABILITIES	
Non-current portion of notes payable	19,984
Capital lease obligations, net of current portion	17,885
Deferred rent concession, net of current portion	--
	37,869
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, 78,087,261 and 61,705,019 shares issued and outstanding	78,088
Common stock to be issued (none and 14,479,093 shares)	--
Additional paid-in capital	16,404,768
Deferred compensation	--
Accumulated deficit	(19,342,020)
Total stockholders' deficiency	(2,859,164)
Total liabilities and stockholders' deficiency	$ 675,912

See accompanying notes to condensed consolidated financial statements.

SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the three and nine months ended September 30, 2006 and 2005 (Unaudited)

	For the three months ended September 30,		For the nine m Septembe
	2006	2005	2006
Sales, net	$ 288,379	$ 347,061	$ 1,105,639
Cost of goods sold	183,412	191,545	670,785
Gross profit	104,967	155,516	434,854
Operating expenses	428,349	405,733	1,515,335
Amortization of discount on notes payable	108,721	86,876	376,807
Stock-based compensation costs	48,456	--	163,806
Total expenses	585,525	492,609	2,055,948
Gain on sale of equipment to related party	--	--	16,905
Net loss	$ (480,558)	$ (337,093)	$ (1,604,189)
Loss per common share, basic and diluted	$ (.01)	$ (.01)	$ (.02)
Weighted average shares outstanding, basic and diluted	77,416,571	59,279,241	73,374,571

See accompanying notes to condensed consolidated financial statements.

SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN
STOCKHOLDERS' DEFICIENCY For the nine months ended
September 30, 2006 (Unaudited)

	Common Stock		Common Stock to be issued		
	Shares	Amount	Shares	Amount	Additiona paid-in capital
Balance January 1, 2006	61,705,019	$ 61,705	14,479,093	$550,000	$15,456,8
Cancellation of stock options	--	--	--	--	(26,5
Stock option expense	--	--	--	--	118,8
Compensatory stock issued	211,625	212	--	--	44,6
Warrants issued with notes payable	--	--	--	--	172,3
Stock issued for warrants exercised in prior year	14,479,093	14,479	(14,479,093)	(550,000)	535,5
Stock issued for settlement of notes payable	1,691,524	1,692	--	--	103,0
Net loss	--	--	--	--	
Balance September 30, 2006	78,087,261	$ 78,088	--	$ --	$ 16,404,7

	Total
Balance January 1, 2006	$ (1,695,890)
Cancellation of stock options	--
Stock option expense	118,898
Compensatory stock issued	44,908
Warrants issued with notes payable	172,389
Stock issued for warrants exercised in prior year	--
Stock issued for settlement of notes payable	104,720
Net loss	(1,604,189)
Balance	

September 30, 2006	$ (2,859,164)

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEM SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH
FLOWS For the nine months ended September 30, 2006 and 2005 (Unaudited)

	2006	
Cash flows from operating activities:		
Net loss	$(1,604,189)	$(
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock-based compensation costs	163,806	
Depreciation and amortization	53,259	
Amortization of discount on notes payable	376,807	
Amortization of deferred compensation	--	
Gain on sale of property and equipment	(16,905)	
Changes in operating assets and liabilities:		
Accounts receivable	76,371	
Inventory	38,306	
Prepaids and other current assets	44,046	
Deferred rent	(4,500)	
Accounts payable and accrued expenses	434,028	
Net Cash Used in Operating Activities	(438,971)	
Cash flows from investing activities:		
Purchase of property and equipment	(1,553)	
Proceeds from sale of property and equipment	79,200	
Net Cash Provided by (Used in) Financing Activities	77,647	
Cash flows from financing activities:		
Proceeds from notes payable	265,000	
Principal payments on notes payable	(38,440)	
Principal payments on capital leases	(6,551)	
Net Cash Provided by Financing Activities	220,009	
Net decrease in cash and cash equivalents	(141,315)	
Cash and cash equivalents, beginning of period	172,732	
Cash and cash equivalents, end of period	$ 31,417	$

Supplemental disclosure of cash flow information Cash paid for:		
Interest	$ 21,049	$
Taxes	$ --	$
Non-cash investing and financing activities:		
Cancellations and forfeitures of stock options	$ 26,598	$
Compensatory stock issued	--	
Warrants exercised by shareholders from merger	--	
Accrued interest added to notes payable principal	4,720	
Discount related to warrants and convertible notes	172,389	
Conversion of notes payable	104,720	

See accompanying notes to condensed consolidated financial statements.

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SENSOR SYSTEMS SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 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

Sensor Systems Solutions, Inc. (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 specifically designed to the customers needs.

Going concern

The Company incurred a net loss of $1,604,189 and a negative cash flow from operations of $438,971 for the nine months ended September 30, 2006, and had a working capital deficiency of $3,045,268 and a stockholders' deficiency of $2,859,164 at September 30, 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 September 30, 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 the remainder of the year.

Principles of consolidation

The consolidated financial statements for the three and nine months ended September 30, 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 effective January 1, 2006. SFAS 123R also supersedes APB No. 25 and amends SFAS No. 95, "Statement of Cash Flows". Effective January 1, 2006, SFAS 123R requires that the Company measure the cost of employee services received in exchange for equity awards based on the grant date fair value of the awards, with the cost to be recognized as compensation expense in the Company's financial statements over the vesting period of the awards.

Accordingly, the Company will recognize compensation cost for equity-based compensation for all new or modified grants issued after December 31, 2005. Although SFAS 123R would also require the Company to recognize the unvested portion of the grant date fair value of awards issued prior to adoption of SFAS 123R based on the fair values previously calculated for disclosure purposes over the remaining vesting period of the outstanding stock options and warrants, there are none because all options issued prior to January 1, 2006 were cancelled in the first quarter of 2006 (see Note 7).

The Company is using the modified prospective method in which compensation cost is recognized beginning with the effective date based on the requirements of SFAS 123R for all share-based payments granted after the effective date.

The total stock-based compensation expense for the three and nine months ended September 30, 2006 was $48,456 and $163,806, respectively, of which $48,456 and $118,898 was from stock options granted during 2006. The balance was from common shares issued in lieu of cash. At September 30, 2006, the unamortized value of these option awards was $172,735 which will be amortized in future periods as the options vest. The fair value of options was estimated on the date of grant

using the Black-Scholes option pricing model with the following weighted-average assumptions for the periods indicated.

	Three months ended Sept. 30, 2006	Nine months ended Sept. 30, 2006
Dividend yield	0%	0%
Risk-free interest rate	4.9%	4.9%
Expected volatility	230%	212%
Expected life of options (years)	6.0	5.7

Prior to the adoption of SFAS 123R, the Company elected to account for its employee and director stock-based awards under the provisions of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees" and it provided the pro-forma disclosures required under SFAS 123 and SFAS 148. Pro-forma information for the three and nine months ended September 30, 2005 is as follows:

	Three months ended Sept. 30, 2005	Nine months ended Sept. 30, 2005
Net loss	$ (337,093)	$(1,158,375)
Add: Stock-based expense included in net loss	10,704	34,588
Deduct: Fair value based stock-based expense	(13,200)	(39,160)
Pro forma net loss	$ (335,589)	$(1,162,947)
Basic and diluted earnings per share:		
As reported	$ (.01)	$ (.02)
Pro forma under SFAS No. 123	$ (.01)	$ (.02)

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 September 30, 2006 and 2005, the Company had granted stock options for 1,610,000 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 September 30, 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.

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 or the cumulative effect of the change. In the event of such impracticality, SFAS 154 provides for other means of application. In the event the Company changes accounting principles, it will evaluate the impact of SFAS 154.

FASB Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements, issued in September 2006, establishes a formal framework for measuring fair value under GAAP. It defines and codifies the many definitions of fair value included among various other authoritative literature, clarifies and, in some instances, expands on the guidance for implementing fair value measurements, and increases the level of disclosure required for fair value measurements. Although SFAS No. 157 applies to and amends the provisions of existing FASB and AICPA pronouncements, it does not, of itself, require any new fair value measurements, nor does it establish valuation standards. SFAS No. 157 applies to all other accounting pronouncements requiring or permitting fair value measurements, except for; SFAS No. 123 (R), share-based payment and related pronouncements, the practicability exceptions to fair value determinations allowed by various other authoritative pronouncements, and AICPA Statements of Position 97-2 and 98-9 that deal with software revenue recognition. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years.

NOTE 2 SIGNIFICANT EVENT

On September 14, 2006, the Company was evicted from the premises it leases at 45 Parker Avenue in Irvine, CA (see Note 8) by The Irvine Company, the lessor of the property, for nonpayment of rent. The Company is attempting to obtain additional funding to pay the back rent and move back in. Alternatively, the Company may seek a suitable other location for its operations (see Note 9 - Subsequent Events).

NOTE 3 INVENTORY

Inventory consists of the following at:

	September 30, (Unaudited
Raw materials	$ 133,6
Finished goods	130,2
	$ 263,8

NOTE 4 NOTES PAYABLE

Notes payable consist of the following at September 30, 2006 and December 31, 2005:

	September 2006 (Unaudit
Two lines of credit, unsecured, interest payable monthly at 10.75% and 11.5% per annum, due on demand.	$ 86,1
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%).	29,9
Note payable, unsecured, interest payable monthly at 10% per annum, payable as a percentage of any future private or public stock offerings.	90,0
Five notes payable (four at December 31,2006), secured by all assets of the Company, interest at 8% per annum, payable at various maturities through July 20, 2007. One note for $200,000 was due February 21, 2006 and was converted into a note due August 21, 2006. The other notes for $64,800, $32,400 and $49,707 were due on April 18, 2006, April 20, 2006 and May 30, 2006, respectively. The Company is currently negotiating an extension of these notes. The fifth note is for $30,000 and is due July 20, 2007. 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 $348,965, has been recorded as loan discount costs and is being amortized over the life of the respective note as additional interest cost.	376,9

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. During the three months ended September 30, 2006, $50,000 of this note was converted into 1,354,524 shares of common stock.	750,0
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.	200,0
Less, remaining debt discount	(89,1
	1,443,8
Less, non-current portion of notes	(19,9
	$ 1,423,8

NOTE 5 NOTES PAYABLE, RELATED PARTIES

Notes payable to related parties consist of the following at September 30, 2006 and December 31, 2005:

	September 2006 (Unaudite
Note payable to the sister of the Company's Chief Executive Officer, secured by all assets of the Company, interest at 14.25% per annum, due December 31, 2004. The note payable was originally issued by Advanced Custom Sensors, Inc. (ACSI), which merged with the company in 2004. In connection with the note payable, ACSI issued warrants expiring September 17, 2008, to purchase 190,665 shares of ACSI's common stock at $.50 per share (The ACSI warrant is convertible into 5,372,940 shares of the Company's stock). The intrinsic value of the warrant ($190,665) has been recorded as loan discount costs and is being amortized over the life of the note as additional interest cost. The Company is currently negotiating an extension of this note.	$ 190,6
Note payable to the sister of the Company's Chief Executive Officer, secured by all assets of the Company, interest at 10.0% per annum, due March 15, 2005. The note payable was originally issued by ACSI in 2003, at which time ACSI issued a warrant expiring September 17, 2008, to purchase 100,000 shares of stock at $.50 per share (the ACSI warrant is convertible into 2,817,215 shares of the Company's common stock). The intrinsic value of the original warrant ($100,000) was recorded as a loan discount cost, and was amortized over the life of the original note as additional interest cost. The original note was due September 16, 2004. On September 16, 2004, a new note was issued to replace the original note. At maturity, the new note is convertible at the holder's option at a	110,0

conversion price equal to 80% of the weighted average price of the common stock for the 30 trading days immediately preceding the conversion date. In addition, the 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 intrinsic value of the beneficial conversion feature of the note and warrants, valued at $48,125, has been recorded as loan discount costs and is being amortized over the life of the note as additional interest cost. The Company is currently negotiating an extension of this note.

Note payable to an employee of the Company, secured by all assets of the Company, interest at 8.0%per annum, due May 30, 2006. At maturity, the note is 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, the 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 intrinsic value of the beneficial conversion feature of the note and warrants, valued at $13,886, has been recorded as loan discount costs and is being amortized over the life of the note as additional interest cost.	--
Note payable to shareholder, secured by all assets of the Company, interest at 8.0% per annum at 8.0% per annum, due April 3, 2006. At maturity the note is 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, the 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 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 of $4,720 was converted into 342,000 shares of common stock at maturity.	--
Note payable to shareholder, secured by all assets of the Company, interest at 8.0% per annum at 8.0% per annum, due August 17, 2007. At maturity the note is 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, the 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 intrinsic value of the beneficial conversion feature of the note and warrants, valued at $22,500, has been recorded as loan discount costs and is being amortized over the life of the note as additional interest cost.	35,000
Less, remaining debt discount	(19,812)

$ 315,853
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NOTE 6 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 was not fully operational as of September 30, 2006. USI has incurred cumulative losses at September 30, 2006 of approximately $662,000, including $430,000 for the nine 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.

As of September 30, 2006, the Company also had trade accounts receivable and payable due from and to USI in the amounts of $53,628 and $187,218, respectively. During the nine months ended September 30, 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.

NOTE 7 STOCK OPTIONS

The Company had a stock option plan, which provided for the granting of options to employees, independent representatives and directors of the Company. The Company was authorized to issue 200,000 shares of common stock of Advanced Custom Sensors, Inc. (ACSI) which merged with Sensor System Solutions, Inc. in 2004. The exercise price was fixed by the plan administrator, shares vested over four years upon the optionee's completion of service and the options expired ten years from the date of grant. At January 1, 2006, there were options for 76,000 shares outstanding with an exercise price of $.50. In the first quarter of 2006, the Board of Directors cancelled this plan and all outstanding options. The Board then approved a new stock compensation plan which includes stock options and other forms of stock-based awards. The Company is authorized to issue 5,000,000 shares of common stock under this plan. The first grant of stock options was to the employees whose ACSI stock options were cancelled. They were granted options for 760,000 shares on March 3, 2006 at the closing price on that date with a vesting period of one year.

At September 30, 2006, options outstanding are as follows:

	Shares	Average Exercise Price

Balance at January 1, 2006	76,000	$.50
Cancelled	(76,000)	.50
Replacement options	760,000	.21
Granted	850,000	.19
Exercised	--	
Balance at September 30, 2006	1,610,000	$.20

NOTE 8 COMMITMENTS AND CONTINGENCIES

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 September 30, 2006	Amount
2006 (three months)	$ 3,183
2007	12,732
2008	12,732
2009	3,903
	32,550
Amount representing interest	(4,902)
Present value of minimum lease payments	27,648
Less: Current portion	(9,763)
	$ 17,885

SENSOR SYSTEMS SOLUTIONS, INC. AND SUBSIDIARY
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005 (UNAUDITED)

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 (see Notes 2 and 9).

Future minimum lease commitments for the Company's share under this lease at September 30, 2006 are as follows:

2006 (three months)	$ 64,175
2007	151,095
	$215,270

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NOTE 9 SUBSEQUENT EVENTS

On November 15. 2006, a settlement was reached with The Irvine Company to allow the Company to re-enter the premises and begin limited operations. The settlement calls for a payment of $100,000 to re-enter the premises and $79,040 of back rent by December 15, 2006. The Company's CEO and two other employees went through the premises on November 15, 2006 and determined that all inventory and machinery that was locked up on September 14, 2006 was still there and nothing was damaged or missing and that all items were fully accounted for.

Cornell Capital has agreed to loan the Company $250,000 under a bridge loan to pay the back rent and to fund operations for the short term. Cornell Capital has agreed that once the Company's September 30, 2006 10-QSB is filed, they will advance the funds necessary for the Company to pay The Irvine Company $100,000.

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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 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 14 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.

* 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.

* 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.

* 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 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.

* 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 September 30, 2006 and 2005

Revenues

We generated revenues of $288,379 for the three months ended September 30, 2006, which was a decrease of $58,682 or 17% from $347,061 for the three months ended September 30, 2005. The decrease is primarily the result of being evicted on September 14, 2006 from the premises it leases (see Note 2 to the Consolidated Financial Statements). Revenues will be severely reduced in the fourth quarter as operations were curtailed through November 2006 (see Note 9 to the Consolidated Financial Statements).

Gross Profit

Gross profit for the three months ended September 30, 2006, was $104,967 or

36.4% of revenues, compared to $155,516 or 44.8% for the three months ended September 30, 2005. The $50,549 decrease in gross profit was a result of the decrease in revenue and the higher cost of sales percentage which was due to lower productivity caused by the eviction mentioned above.

Total Expenses

Operating expenses

Operating expenses increased to $428,349 for the three months ended September 30, 2006 compared to $405,733 for the three months ended September 30, 2005. The expenses increased $22,616, primarily as a result of an increase in interest expense and rent, partially offset by lower payroll and insurance costs.

Amortization of discount on notes payable

Amortization of discount on notes payable increased to $108,721 for the three months ended September 30, 2006 compared to $86,876 for the three months ended September 30, 2005. The expense increased $21,845, or 25%, primarily due to the Cornell Capital Partners borrowings of $800,000 in December 2005 and $200,000 in February 2006.

Stock-based compensation costs

During the three months ended September 30, 2006, the Company recorded $48,456 in stock-based compensation costs for options issued to employees during the quarter. There were no stock-based compensation costs in the three months ended September 30, 2005.

Net Loss

Net loss increased to ($480,558) for the three months ended September 30, 2006 compared to ($337,093) for the three months ended September 30, 2005. The $143,465 increase in net loss is due to the increase in operating expenses and the decrease in gross profit.

Nine months Ended September 30, 2006 and 2005

Revenues

We generated revenues of $1,105,639 for the nine months ended September 30, 2006, which was $250,307 or a 29% increase from $855,332 for the nine months ended September 30, 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 nine months ended September 30, 2006, was $434,854 or 39.3% of revenues, compared to $289,943 or 33.9% for the six months ended September 30, 2005. The $144,911 increase in gross profit was generated by the increase in revenue and 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 Expenses

Operating expenses

Operating expenses increased to $1,515,335 for the nine months ended September 30, 2006 compared to $1,169,982 for the nine months ended September 30, 2005. The expenses increased $345,353, primarily as a result of an increase in interest expense, rent, payroll, additional investment in R&D, travel and legal fees.

Amortization of discount on notes payable

Amortization of discount on notes payable increased to $376,807 for the nine months ended September 30, 2006 compared to $278,336 for the nine months ended September 30, 2005. The expense increased $98,471, or 35%, primarily due to the Cornell Capital Partners borrowings of $800,000 in December 2005 and $200,000 in February 2006.

Stock-based compensation costs

During the nine months ended September 30, 2006, the Company recorded $118,898 in stock-based compensation costs for options issued to employees. Another $44,908 was recorded for compensatory stock issued to non-employees for services rendered. There were no stock-based compensation costs in the nine months ended September 30, 2005.

Net Loss

Net loss increased to ($1,604,189) for the nine months ended September 30, 2006 compared to ($1,158,375) for the nine months ended September 30, 2005. The $445,814 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 $1,604,189 and a negative cash flow from operations of $438,971 for the nine months ended September 30, 2006, and had a working capital deficiency of $3,045,268 and a stockholders' deficiency of $2,859,164 at September 30, 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 and received $65,000 in loans during the third quarter. 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.

At September 30, 2006, cash was $31,417 as compared to $172,732 at December 31, 2005. The decrease is due to the negative cash flow from operations, primarily due to the net loss of $1,604,189 reduced by $593,872 in non-cash expenditures for stock-based compensation, amortization of debt discount costs and depreciation and amortization. Changes in operating assets and liabilities contributed an additional $588,251 in cash, primarily from a decrease in accounts payable of $434,028. The cash flows from investing and financing activities totaling $297,656 was not enough to fund the $438,971 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.

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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 September 30, 2006	Amount
2006 (three months)	$ 3,183
2007	12,732
2008	12,732
2009	3,903
	32,550
Amount representing interest	(4,902)
Present value of minimum lease payments	27,648
Less: Current portion	(9,763)
	$ 17,885

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 (see Notes 2 and 9 to the Consolidated Financial Statements).

Future minimum lease commitments for the Company's share under this lease at September 30, 2006 are as follows:

2006 (three months)	$ 64,175
2007	151,095
	$ 215,270

Inflation and Changing Prices

We do not foresee any adverse effects on our earnings as a result of inflation

or changing prices.

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

During the first quarter of 2006, the Company adopted Statement No. 151 (SFAS 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 151 did not have a material impact on the Company's financial condition, results of operations or cash flows.

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 impracticality, SFAS 154 provides for other means of application. In the event the Company changes accounting principles, it will evaluate the impact of SFAS 154.

FASB Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements, issued in September 2006, establishes a formal framework for measuring fair value under GAAP. It defines and codifies the many definitions of fair value included among various other authoritative literature, clarifies and, in some instances, expands on the guidance for implementing fair value measurements, and increases the level of disclosure required for fair value measurements. Although SFAS No. 157 applies to and amends the provisions of

existing FASB and AICPA pronouncements, it does not, of itself, require any new fair value measurements, nor does it establish valuation standards. SFAS No. 157 applies to all other accounting pronouncements requiring or permitting fair value measurements, except for; SFAS No. 123 (R), share-based payment and related pronouncements, the practicability exceptions to fair value determinations allowed by various other authoritative pronouncements, and AICPA Statements of Position 97-2 and 98-9 that deal with software revenue recognition. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years.

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.

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 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 commercially viable level of sales.

From inception through September 30, 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 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.

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 BALACE 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 . 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.

PART II
OTHER INFORMATION

Item 1. Legal Proceedings.

None.

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

On July 20, 2006, the Company issued a note payable for $30,000, secured by all assets of the Company, interest at 8% per annum, payable on July 20, 2007. The note is convertible at the holder's option at a conversion price equal to 70% of the average closing bid price of the common stock for the 30 trading days immediately preceding the conversion date. 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.

On August 17, 2006, the Company issued a note payable for $35,000, secured by all assets of the Company, interest at 8% per annum, payable on August 17, 2007. The note is convertible at the holder's option at a conversion price equal to 70% of the average closing bid price of the common stock for the 30 trading days immediately preceding the conversion date. 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 15, 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.

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

A $47,707 convertible loan matured on May 30, 2006. The Company is currently negotiating an extension of the note.

A $200,000 convertible loan matured on August 21, 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

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: November 17, 2006

/s/ Michael Young

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