

SINGING MACHINE CO INC  
Form 10-Q  
August 14, 2007

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, DC 20549

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (D)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

For quarter ended June 30, 2007

0 - 24968

*Commission File Number*

**THE SINGING MACHINE COMPANY, INC.**  
(Exact Name of Registrant as Specified in its Charter)

DELAWARE  
(State of Incorporation )

95-3795478  
(IRS Employer I.D. No.)

6601 Lyons Road, Building A-7, Coconut Creek, FL 33073  
(Address of principal executive offices)

(954) 596-1000  
(Issuer's telephone number, including area code)

Securities registered pursuant to Section 12 (b) of the Act: None  
Securities registered pursuant to Section 12(g) of the Act: Common Stock, \$.001 Par Value Per Share

Indicate by check mark 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 requirement for the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

**APPLICABLE ONLY TO ISSUES INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:**

Indicated by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities and Exchange Act of 1934 subsequent to the distribution of securities under a plan

confirmed by a court. Yes  No

**APPLICABLE ONLY TO CORPORATE ISSUERS**

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

CLASS	NUMBER OF SHARES OUTSTANDING
Common Stock, \$0.01 par value	29,898,876 as of August 8, 2007

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**THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY**

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**The Singing Machine Company, Inc. and Subsidiaries**  
**CONSOLIDATED BALANCE SHEETS**

	<b>June 30, 2007</b>	<b>March 31, 2007</b>
	(Unaudited)	
<u><b>Assets</b></u>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 1,003,071	\$ 1,188,900
Accounts receivable, net of allowances of \$84,931 and \$61,825, respectively	1,536,490	1,054,371
Due from factor	450,889	109,991
Inventories	2,518,711	2,280,083
Prepaid expenses and other current assets	543,776	521,891
<b>Total Current Assets</b>	<b>6,052,937</b>	<b>5,155,236</b>
<b>Property and Equipment</b> , at cost less accumulated depreciation of \$1,107,316 and \$1,045,119 ,respectively	415,747	446,510
<b>Other Non-Current Assets</b>	56,054	56,054
<b>Total Assets</b>	<b>\$ 6,524,738</b>	<b>\$ 5,657,800</b>
<u><b>Liabilities and Shareholders' Equity</b></u>		
<b>Current Liabilities</b>		
Accounts payable	\$ 1,387,933	\$ 903,243
Accounts payable - related party	954,818	199,316
Accrued expenses	572,873	624,994
Customer credits on account	650,554	594,169
Deferred gross profit on estimated returns	53,245	213,718
Subordinated debt-related parties	225,000	225,000
<b>Total Current Liabilities</b>	<b>3,844,423</b>	<b>2,760,440</b>
<b>Shareholders' Equity</b>		
Preferred stock, \$1.00 par value; 1,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, Class A, \$.01 par value; 100,000 shares authorized; no shares issued and outstanding	-	-
Common stock, \$0.01 par value; 100,000,000 shares authorized; 29,898,876 and 27,286,199 shares issued and outstanding	298,989	272,862
Additional paid-in capital	17,915,486	17,306,342
Accumulated deficit	(15,534,160)	(14,681,844)
<b>Total Shareholders' Equity</b>	<b>2,680,315</b>	<b>2,897,360</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 6,524,738</b>	<b>\$ 5,657,800</b>

*The accompanying notes are an integral part of these financial statements.*

*The Singing Machine Company, Inc. and Subsidiaries*  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
*(Unaudited)*

	<b>For Three Months Ended</b>	
	<b>June 30, 2007</b>	<b>June 30, 2006</b>
<b>Net Sales</b>	\$ 2,446,100	\$ 1,035,876
<b>Cost of Goods Sold</b>	2,106,748	909,404
<b>Gross Profit</b>	339,352	126,472
<b>Operating Expenses</b>		
Selling expenses	163,905	3,770
General and administrative expenses	960,277	1,165,697
Depreciation and amortization	62,197	108,009
<b>Total Operating Expenses</b>	1,186,379	1,277,476
<b>Loss from Operations</b>	(847,027)	(1,151,004)
<b>Other Income (Expenses)</b>		
Other income	-	9,018
Interest expense	(5,289)	(9,102)
<b>Net Other Expenses</b>	(5,289)	(84)
<b>Net Loss</b>	\$ (852,316)	\$ (1,151,088)
<b>Loss per Common Share</b>		
Basic	\$ (0.03)	\$ (0.11)
Diluted	\$ (0.03)	\$ (0.11)
<b>Weighted Average Common and Common Equivalent Shares:</b>		
Basic	29,413,957	10,736,532
Diluted	29,413,957	10,736,532

*The accompanying notes are an integral part of these financial statements.*

**The Singing Machine Company, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

	<b>For Three Months Ended</b>	
	<b>June 30, 2007</b>	<b>June 30, 2006</b>
<b>Cash flows from operating activities</b>		
<i>Net Loss</i>	\$ (852,316)	\$ (1,151,088)
Adjustments to reconcile net loss to net cash and cash equivalents used in operating activities:		
Depreciation and amortization	62,197	108,009
Change in inventory reserve	(14,267)	(6,853)
Change in allowance for bad debts	(18,684)	-
Stock compensation	20,891	52,692
Deferred gross profit on estimated sales returns	(160,473)	(138,039)
<i>Changes in assets and liabilities:</i>		
(Increase) Decrease in:		
Accounts receivable	(463,435)	129,151
Inventories	(224,361)	88,846
Prepaid expenses and other assets	(21,885)	(304,975)
Other non-current assets	-	2,436
Increase (Decrease) in:		
Accounts payable	484,692	503,325
Accounts payable - related party	755,502	-
Accrued expenses	(52,123)	(155,780)
Customer credits on account	56,384	(595,654)
Net cash used in operating activities	(427,878)	(1,467,930)
<b>Cash flows from investing activities</b>		
Purchase of property and equipment	(31,434)	(71,550)
Receipt of restricted cash	-	268,405
Net cash (used in) provided by investing activities	(31,434)	196,855
<b>Cash flows from financing activities</b>		
(Retention by) borrowings from factor, net	(340,898)	16,162
Proceeds from issuance of stock	614,381	1,000,000
Net cash provided by financing activities	273,483	1,016,162
<b>Change in cash and cash equivalents</b>	<b>(185,829)</b>	<b>(254,913)</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>1,188,900</b>	<b>423,548</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 1,003,071</b>	<b>\$ 168,635</b>
<b>Supplemental Disclosures of Cash Flow Information:</b>		
Cash paid for Interest	\$ 5,341	\$ 16,232
<b>Non-Cash Financing Activities:</b>		
Conversion of loan payable to equity	\$ -	\$ 2,000,000

*The accompanying notes are an integral part of these financial statements.*



**THE SINGING MACHINE COMPANY, INC AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - SUMMARY OF ACCOUNTING POLICIES**

**OVERVIEW**

The Singing Machine Company, Inc., a Delaware corporation (the "Company," "SMC", or "The Singing Machine"), and wholly-owned Macau Subsidiary, SMC (Comercial Offshore De Macau) Limitada ("Macau Subsidiary") are primarily engaged in the development, marketing, and sale of consumer karaoke audio equipment, accessories, musical instruments and musical recordings. In July 1994, we formed a wholly owned subsidiary in Hong Kong, known as International SMC (HK) Ltd. ("International SMC" or "Hong Kong subsidiary"), to coordinate our engineering, production, logistics and financial operations in China. In September 2006, International SMC was sold to See Bright Investments Limited, a non-related third party. In December 2005, we formed a wholly-owned subsidiary SMC (Commercial Offshore De Macau) Limitada in Macau, China ("SMC Macau" or "Macau subsidiary"), to provide shipping, engineering and sourcing support for Singing Machine Subsidiaries. The products are sold directly to distributors and retail customers.

The preparation of The Singing Machine's 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 at the date of the financial statements and revenues and expenses during the period. Future events and their effects cannot be determined with absolute certainty; therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the Company's financial statements. Management evaluates its estimates and assumptions continually. These estimates and assumptions are based on historical experience and other factors that are believed to be reasonable under the circumstances.

**THE MANAGEMENT OF THE COMPANY BELIEVES THAT THE FOLLOWING ACCOUNTING POLICIES REQUIRE A HIGH DEGREE OF JUDGEMENT DUE TO THEIR COMPLEXITY:**

**COLLECTIBILITY OF ACCOUNTS RECEIVABLE.** The Singing Machine's allowance for doubtful accounts is based on management's estimates of the creditworthiness of its customers, current economic conditions and historical information, and, in the opinion of management, is believed to be an amount sufficient to respond to normal business conditions. Management sets 100% reserves for customers in bankruptcy and other reserves based upon historical collection experience. Should business conditions deteriorate or any major customer default on its obligations to the Company, this allowance may need to be significantly increased, which would have a negative impact on operations.

**RESERVES ON INVENTORIES.** The Singing Machine reduces inventory on hand to its net realizable value on an item-by-item basis when it is apparent that the expected realizable value of an inventory item falls below its original cost. A charge to cost of sales results when the estimated net realizable value of specific inventory items declines below cost. Management regularly reviews the Company's investment in inventories for such declines in value.

**INCOME TAXES.** Significant management judgment is required in developing The Singing Machine's provision for income taxes, including the determination of foreign tax liabilities, deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. Management evaluates its ability to realize its deferred tax assets on a quarterly basis and adjusts its valuation allowance when it believes that it is more likely that the asset will not be realized.

The Company follows Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes" ("SFAS No. 109"). Under the asset and liability method of SFAS No. 109, deferred tax assets and liabilities are recognized for



the future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under SFAS No. 109, 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. If it is more likely than not that some portion of a deferred tax asset will not be realized, a valuation allowance is recognized.

Due to the change of control of the Company in June 2006, the net operating loss carry over is subject to the IRS Section 382 limitation. As of June 30, 2007 and March 31, 2007, The Singing Machine had gross deferred tax assets of approximately \$3.0 million and \$2.7 million, respectively, against which the Company recorded valuation allowances totaling approximately \$3.0 million and \$2.7 million, respectively.

The Company files separate tax returns for the parent in the United States and for the Macau Subsidiary. The Macau Subsidiary has received approval from the Macau government to operate its business as a Macau Offshore Company (MOC), and is exempt from the Macau income tax. For the quarters ended June 30, 2007 and 2006, the Company recorded no tax provision. The Company has now exhausted its ability to carry back any further losses and therefore will only be able to recognize tax benefits to the extent that it has future taxable income.

**OTHER ESTIMATES.** The Singing Machine makes other estimates in the ordinary course of business relating to sales returns and allowances, warranty reserves, and reserves for promotional incentives. Historically, past changes to these estimates have not had a material impact on the Company's financial condition. However, circumstances could change which may alter future expectations.

**THE FOLLOWING ARE THE COMPANY'S REMAINING ACCOUNTING POLICIES:**

**PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements include the accounts of The Singing Machine Company, Inc., its wholly-owned Macau Subsidiary, SMC (Comercial Offshore De Macau) Limitada (“Macau Subsidiary”), The Singing Machine Holdings Ltd. (a B.V.I. company), and its former wholly-owned Hong Kong subsidiary International SMC (HK) Limited through date of sale. All inter-company accounts and transactions have been eliminated in consolidation for all periods presented.

**FOREIGN CURRENCY TRANSLATION**

The functional currency of the Macau Subsidiary is the Hong Kong dollar. The financial statements of the subsidiaries are translated to U.S. dollars using year-end rates of exchange for assets and liabilities, and average rates of exchange for the year for revenues, costs, and expenses. Net gains and losses resulting from foreign exchange transactions and translations were not material during the periods presented.

**CASH AND CASH EQUIVALENTS**

The Company considers all highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents. Cash and cash equivalent balances at June 30, 2007 and March 31, 2007 were \$1,003,071 and \$1,188,900, respectively.

**CONCENTRATION OF CREDIT RISK**

The Company maintains cash balances in foreign financial institutions. Such balances are not insured. The uninsured amounts at June 30, 2007 and March 31, 2007 are \$401,821 and \$240,682, respectively.

**INVENTORY**

Inventories are comprised of electronic karaoke equipment, accessories, and compact discs and are stated at the lower of cost or market, as determined using the first in, first out method.

**SHIPPING AND HANDLING COSTS**

Shipping and handling costs are classified as a separate component of operating expenses and those billed to customers are recorded as reduction of the operating expenses in the statement of operations.

**PROPERTY AND EQUIPMENT**

Property and equipment are stated at cost, less accumulated depreciation and amortization. Expenditures for repairs and maintenance are charged to expense as incurred. Depreciation is provided for in amounts sufficient to relate the cost of depreciable assets to their estimated useful lives using accelerated and straight-line methods.

**REVENUE RECOGNITION**

Revenue from the sale of equipment, accessories, and musical recordings are recognized upon the later of (a) the time of shipment or (b) when title passes to the customers and all significant contractual obligations have been satisfied and collection of the resulting receivable is reasonably assured. Revenues from sales of consigned inventory are recognized upon sale of the product by the consignee. Net sales are comprised of gross sales net of actual and

estimated future returns, discounts and volume rebates.

## **STOCK BASED COMPENSATION**

The Company began to apply the provisions of SFAS No. 123 (revised 2004), Share-Based Payments ("SFAS 123 (R)"), starting on January 1, 2006. SFAS 123 (R) which became effective after June 15, 2005, replaces SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion ("APB") No. 25, Accounting for Stock Issued to Employees. SFAS 123 (R) requires all share-based payments to employees including grants of employee stock options, be measured at fair value and expensed in the consolidated statement of operations over the service period (generally the vesting period). Upon adoption, the Company transitioned to SFAS 123 (R) using the modified prospective application, whereby compensation cost is only recognized in the consolidated statements of operations beginning with the first period that SFAS 123 (R) is effective and thereafter, with prior periods' stock-based compensation still presented on a pro forma basis. Under the modified prospective approach, the provisions of SFAS 123 (R) are to be applied to new employee awards and to employee awards modified, repurchased, or cancelled after the required effective date. Additionally, compensation cost for the portion of employee awards for which the requisite service has not been rendered that are outstanding as of the required effective date shall be recognized as the requisite service is rendered on or after the required effective date. The compensation cost for that portion of employee awards shall be based on the grant-date fair value of those awards as calculated for either recognition or pro-forma disclosures under SFAS 123. The Company continues to use the Black-Scholes option valuation model to value stock options. As a result of the adoption of SFAS 123 (R), the Company recognized a charge of \$6,790 (included in selling, general and administrative expenses) for the three months ended June 30, 2007 associated with the expensing of stock options. For the three months ended June 30, 2006, the stock option expense was \$52,692. Employee stock option compensation expense in fiscal years 2007 and 2006 includes the estimated fair value of options granted, amortized on a straight-line basis over the requisite service period for the entire portion of the award.

The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option-pricing model with the assumptions outlined below. For the quarter ended June 30, 2007, the Company took into consideration guidance under SFAS 123 (R) and SEC Staff Accounting Bulletin No. 107 (SAB 107) when reviewing and updating assumptions. The expected volatility is based upon historical volatility of our stock and other contributing factors. The expected term is based upon observation of actual time elapsed between date of grant and exercise of options for all employees. Previously such assumptions were determined based on historical data.

- For the three months ended June 30, 2007: expected dividend yield 0%, risk-free interest rate of 4.92%, volatility of 90.77% and expected term of three years.
- For the three months ended June 30, 2006: expected dividend yield 0%, risk-free interest rate of 5.1%, volatility 91% and expected term of three years.

## **ADVERTISING**

Costs incurred for producing and publishing advertising of the Company, are charged to operations as incurred. The Company has entered into cooperative advertising agreements with its major clients that specifically indicated that the client has to spend the cooperative advertising fund upon the occurrence of mutually agreed events. The percentage of the cooperative advertising allowance ranges from 2% to 5% of the purchase. The clients have to advertise the Company's products in the client's catalog, local newspaper and other advertising media. The client must submit the proof of the performance (such as a copy of the advertising showing the Company's products) to the Company to request for the allowance. The client does not have the ability to spend the allowance at their discretion. The Company believes that the identifiable benefit from the cooperative advertising program and the fair value of the advertising benefit is equal or greater than the cooperative advertising expense. Advertising expense for the three months ended June 30, 2007 and 2006 was \$60,244 and \$4,476, respectively.

## **RESEARCH AND DEVELOPMENT COSTS**

All research and development costs are charged to results of operations as incurred. These expenses are shown as a component of selling, general and administrative expenses in the consolidated statements of operations. For the three months ended June 30, 2007 and 2006, these amounts totaled \$1,090 and \$25,588, respectively.

## **FAIR VALUE OF FINANCIAL INSTRUMENTS**

SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," requires disclosures of information about the fair value of certain financial instruments for which it is practicable to estimate that value. For purposes of this disclosure, the fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation.

The carrying amounts of the Company's short-term financial instruments, including accounts receivable, accounts payable and accrued expenses approximates fair value due to the relatively short period to maturity for these instruments.

## **RECLASSIFICATIONS**

Certain prior year amounts have been reclassified to conform to the current year presentation.

## **RECENT ACCOUNTING PRONOUNCEMENTS**

In July 2006, the FASB issued FASB Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, Accounting for Income Taxes." FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on de-recognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The interpretation applies to all tax positions related to income taxes subject to FASB Statement No. 109.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurement which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurement. Companies are required to adopt the new standard for fiscal periods beginning after November 15, 2007. We are currently evaluating the impact of this standard on our Consolidated Financial Statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - including an amendment to FAS 115. This statement permits companies to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. Companies are required to adopt the new standard for fiscal periods beginning after November 15, 2007. We are currently evaluating the impact of this standard on our Consolidated Financial Statements.

**NOTE 2 - INVENTORIES**

Inventories are comprised of the following components:

	June 30, 2007	March 31, 2007
Finished Goods	\$ 2,704,887	\$ 2,334,381
Inventory in Transit	-	144,550
Less: Inventory Reserve	(186,176)	(198,848)
<b>Total Inventories</b>	<b>\$ 2,518,711</b>	<b>\$ 2,280,083</b>

Inventory consigned to customers at June 30, 2007 and March 31, 2007 were \$459,298 and \$418,598, respectively.

**NOTE 3 - ACCOUNTS RECEIVABLE FACTORING AGREEMENT**

On August 4, 2004, the Company entered into a 3-year factoring agreement with Crestmark Bank in Detroit, Michigan. The agreement allows the Company, at the discretion of Crestmark, to factor its outstanding receivables, with recourse, up to a maximum of the lesser of approximately \$2.5 million or 70% of eligible accounts receivable. The Company pays 1% of gross receivables in fees with a \$9,000 minimum maintenance fee per month. The average balance of the line will be subject to interest payable on a monthly basis at the prime rate plus 2% (10.25% at June 30, 2007). The agreement contains a liquidated damages fee for early termination by the Company, which equals \$9,000 for each remaining month of the contract term.

The Company granted Crestmark Bank a senior security interest in all of the Company's accounts receivables and inventory in the United States. The related party loan holders have subordinated their debt to the Crestmark Bank debt.

As of June 30, 2007 and March 31, 2007, the outstanding amounts due from Crestmark bank for factoring were \$450,889 and \$109,991, respectively. The amount represents excess of customer payments received by Crestmark Bank over advances made to the Company.

The agreement with Crestmark Bank expired, without renewal, on August 1, 2007. The Company executed an agreement with CIT on August 13, 2007 to factor its receivables. CIT assumes the credit risk on approved accounts (factor risk accounts). For non-approved accounts, the Company will assume the credit risk (client risk accounts). The factoring fees, for the client risk accounts, are .3% of the gross invoice. For the factor risk accounts, the fees are .55% of the gross invoice. The annual minimum charge is \$24,000. The agreement will expire August 2008. After that date, each party will have to give 60 days written notice to terminate the agreement. CIT does not advance funds to the Company directly. The Company is currently working with a bank in Hong Kong to set up a bank facility that will advance funds to the Company based upon CIT's purchases of the Company's accounts receivable. CIT will submit all funds collected directly to the bank in Hong Kong. The Company expects to finalize this banking agreement in September 2007.

**NOTE 4 - PROPERTY AND EQUIPMENT**

A summary of property and equipment is as follows:

USEFUL LIFE	June 30, 2007	March 31, 2007
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Computer and office equipment	5 years	\$	453,533	\$	440,946
Furniture and fixtures	5-7 years		220,171		220,171
Leasehold improvement	*		209,003		209,004
Molds and tooling	3 years		640,356		621,508
			1,523,063		1,491,629
Less: Accumulated depreciation			(1,107,316)		(1,045,119)
		\$	415,747	\$	446,510

\* Shorter of remaining term of lease or useful life

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#### **NOTE 5 - RELATED PARTY LOANS**

The related party loans as of June 30, 2007, which total \$225,000 are due to a director and an individual and currently bear interest at 5.5%. The balance of the loans is due on demand and is subordinated to the loan with Crestmark Bank (See Note 3).

#### **NOTE 6 - CUSTOMER CREDITS ON ACCOUNT**

Customer credits on account represent customers that have received credits in excess of their accounts receivable balance. These balances were reclassified for financial statement purposes as current liabilities until paid or applied to future purchases.

#### **NOTE 7 - COMMITMENTS AND CONTINGENCIES**

#### **LEGAL MATTERS**

**SYBERSOUND RECORDS, INC. V. UAV CORPORATION; MADACY ENTERTAINMENT L.P., AUDIO STREAM, INC., TOP TUNES, INC., SINGING MACHINE, INC., BCI ECLIPSE COMPANY, LLC, AMOS ALTER, DAVID ALTER, EDWARD GOETZ, DENNIS NORDEN, FRANK ROBERTSON, DOUGLAS VOGT AND RICHARD VOGT (UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA, CV05-5861 JFW); (UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT (USCA DOCKET NO. 06-55221)**

The federal court action filed on August 11, 2005 alleged violation of the Copyright Act and the Lanham Act by the defendants, and claims for unfair competition under California law. Sybersound was joined in the complaint by several publisher owners of musical compositions who alleged copyright infringement against all the defendants *except* The Singing Machine Company, Inc. On November 7, 2005, the district court ordered the publisher plaintiffs' copyright claims severed from the case. The Singing Machine Company, Inc. is not a party to the severed cases.

In September 2005, the defendants, including The Singing Machine Company, Inc., filed multiple motions to dismiss the original complaint. In October 2005, Sybersound filed a motion for summary judgment. On January 6, 2006, the court granted the motions of the defendants and denied the plaintiff's motion, thereby dismissing the case against the defendants, including The Singing Machine Company, Inc., with prejudice. The plaintiff Sybersound thereafter appealed the decision to the Ninth Circuit Court of Appeals. The case is currently under review by the appellate court.

Despite the confidence of The Singing Machine Company, Inc. that the ruling in its favor at the district court level will be affirmed on appeal, it is not possible to predict such outcomes with any degree of certainty.

The Company is also subject to various other legal proceedings and other claims that arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability, if any, in excess of applicable insurance coverage, is not likely to have a material effect on the financial condition, results of operations or liquidity of the Company. However, as the outcome of litigation or other legal claims is difficult to predict, significant changes in the range of possible loss could occur, which could have a material impact on the Company's operations.

#### **NON-COMPLIANCE NOTICE FROM AMEX**

On September 6, 2006, the Company received notice from The American Stock Exchange (the "Amex") that the Company has fallen below the continued listing standards of the Amex and that its listing is being continued pursuant to an extension.



For the fiscal years ended March 31, 2007 and March 31, 2006, the Company was not in compliance with Section 1003(a)(ii) of the Amex Company Guide with shareholders' equity of less than \$4,000,000 and net losses in three of its four most recent fiscal years.

In order to maintain its Amex listing, the Company was required to submit a Revised Plan to the American Stock Exchange by October 2, 2006 advising the Amex of actions it will take, which may allow it to regain compliance with all of the Exchange's continued listing standards within a maximum of 18 months from July 18, 2005. The Revised Plan will supplement the Plan originally submitted to the American Stock Exchange on August 18, 2005, as required under a notice of non-compliance announced by The Singing Machine on July 22, 2005. The Revised Plan was submitted by the Company prior to the deadline of October 2, 2006. As of August 14, 2007 the Company is still not in compliance with Amex continuing listing requirement and waiting for Amex's decision.

The Listings Qualifications Department will evaluate the Revised Plan, including any supplemental information provided, and make a determination as to whether the Company has made a reasonable demonstration in the Revised Plan of an ability to regain compliance. If the Revised Plan is accepted, the Company may be able to continue its listing during the plan period, during which time it will be subject to periodic review to determine whether it is making progress consistent with the Revised Plan. The Company may be subject to delisting proceedings if the Revised Plan is not accepted, or if the Revised Plan is accepted but the Company is not in compliance with all of the Exchange's continued listing standards within the time frame provided or does not make progress consistent with the Revised Plan during the plan period.

The Company was previously added to the list of issuers that are not in compliance with the Amex's continued listing standards, and the Company's trading symbol SMD remains subject to the extension ".BC" to denote its noncompliance. This indicator will remain in effect until such time as the Company has regained compliance with all applicable continued listing standards.

**LEASES**

The Company has entered into various operating lease agreements for office and warehouse facilities in Coconut Creek, Florida, Compton, California and Macau. The leases expire at varying dates. Rent expense for the three months ended June 30, 2007 and 2006 was \$59,602 and \$141,983, respectively.

In addition, the Company maintains various warehouse equipment and computer equipment operating leases.

Future minimum lease payments under property and equipment leases with terms exceeding one year as of June 30, 2007 are as follows:

For period	Property Lease	Equipment Lease
Less than 1 year	\$ 464,343	\$ 9,888
1 - 3 years	11,822	22,428
	\$ 476,165	\$ 32,316

**NOTE 8 - STOCKHOLDERS' EQUITY****COMMON STOCK ISSUANCES**

During the three months ended June 30, 2007 and 2006, the Company issued 2,612,677 and 12,875,536 shares of its common stock, respectively.

Included in these shares issued during the three months ended June 30, 2007, the Company issued 112,677 shares of common stock to various employees, as well as directors, at prices ranging from \$.32 per share to \$.93 per share according to employee stock option agreements.

On April 16, 2007, 2,500,000 warrants at \$0.233 were exercised by koncept International Limited, a subsidiary of Starlight, and the Company received a total of \$582,500.

On June 25, 2006, the Company issued 12,875,536 shares of common stock to koncept International Limited, a subsidiary of Starlight for a \$3 million investment (\$.233 per share).

**EARNINGS PER SHARE**

In accordance with SFAS No. 128, "Earnings per Share", basic (loss) earnings per share are computed by dividing the net (loss) earnings for the year by the weighted average number of common shares outstanding. Diluted earnings per share is computed by dividing net earnings for the year by the weighted average number of common shares outstanding including the effect of common stock equivalents.

For the three months ended June 30, 2007 and 2006, 3,538,858 and 6,167,555 common stock equivalents were not included in the computation of diluted earnings per share as their effect would have been anti-dilutive.

**STOCK OPTIONS**

On June 1, 2001, the Board of Directors approved the 2001 Stock Option Plan ("Plan"), which replaced the 1994 Stock Option Plan, as amended, (the "1994 Plan"). The Plan was developed to provide a means whereby directors and selected employees, officers, consultants, and advisors of the Company may be granted incentive or non-qualified

stock options to purchase common stock of the Company. As of June 30, 2007, the Plan is authorized to grant options up to an aggregate of 1,950,000 shares of the Company's common stock and up to 300,000 shares for any one individual grant in any quarter. As of June 30, 2007, the Company had granted 1,512,325 options under the Year 2001 Plan, leaving 437,675 options available to be granted. As of June 30, 2007, the Company had 13,050 options issued and no options available to be granted under the 1994 Plan, since the 1994 Plan has expired (after 10 years).

The exercise price of employee common stock option issuances in the quarters ended June 2007 and 2006 was equal to the fair market value on the date of grant. Accordingly, no compensation cost has been recognized for options issued under the Plan in these years prior to June 15, 2006. The Company adopted SFAS 123(R) for the reporting period ending after June 15, 2005 and recognized the fair value of the stock option as part of the general and administration expenses. The amount of \$6,790 was recorded as part of the general and administrative expenses for the quarter ended June 30, 2007. The amount of \$52,692 was recorded as part of the general and administrative expenses for the three months ended June 30, 2006.

**STOCK WARRANTS**

As of June 30, 2007, the Company had a total of 2,500,000 stock purchase warrants outstanding. The exercise price of these warrants range from \$0.28 to \$0.35. The expiration date of these warrants range from July 25, 2009 to July 26, 2010.

**NOTE 9 - SEGMENT INFORMATION**

The Company operates in one segment and maintains its records accordingly. The majority of sales to customers outside of the United States for the three months ended June 30, 2007 were made by the Macau Subsidiary. The majority of sales to customers outside of the United States for the three months ended June 30, 2006 were made by International SMC (HK) Limited, the Company's former Hong Kong Subsidiary. Sales by geographic region for the period presented are as follows:

	<b>FOR THE THREE MONTHS ENDED</b>	
	June 30,	
	2007	2006
North America	\$ 1,358,845	\$ 554,436
Europe	789,420	461,864
Others	297,835	19,576
	\$ 2,446,100	\$ 1,035,876

The geographic area of sales is based primarily on the location where the product is delivered.

**NOTE 10 - RELATED PARTY TRANSACTIONS**

koncept International Limited, a subsidiary of Starlight International Holding Ltd, invested \$3 million in the Company. The investment was approved by the American Stock Exchange on July 25, 2006. Currently, koncept owns approximately 51% of the Company's outstanding common stock.

The Company also purchased products from Starlight Marketing Macao, a subsidiary of Starlight International Holding Ltd. The purchases from Starlight for the quarter ended June 30, 2007 were \$613,080. In addition, the Company also purchased molds and tooling from Starlight in the amount of \$269,700 in fiscal 2007 and is included in Property and Equipment in the accompanying Consolidated Balance Sheets.

On August 1, 2006, the Company entered into a service agreement with Starlight Electronics Co., Ltd, a subsidiary of Starlight International Holding Ltd, to provide shipping and engineering service to the Company at a charge of \$25,000 per month. Beginning on April 16, 2007, the monthly charge was increased to \$29,000 due to the hiring of additional staff. For the three months ended June 30, 2007, this service charge was \$85,000 and is included in the general and administrative expenses in the accompanying Consolidated Statements of Operations.

In addition, on October 1, 2006 the Company entered into a warehouse service agreement with Starlight Industrial Holding LTD, to provide them with warehousing services at the Company's Compton, California warehouse at a monthly service charge of \$26,000. The amount paid to the Company was \$78,000 for the three months ended June 30, 2007. This amount was used to offset the Company's rent expense for the warehouse and is shown in the accompanying Consolidated Statements of Operations as a component of general and administrative expenses.

The amount due to Starlight and its subsidiary as of June 30, 2007 was \$954,818.

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**FORWARD-LOOKING STATEMENTS**

The following discussion should be read in conjunction with the Financial Statements and Notes thereto. Our fiscal year ends March 31. This document contains certain forward-looking statements including, among others, anticipated trends in our financial condition and results of operations and our business strategy. (See Part II, Item 1A, "Risk Factors "). These forward-looking statements are based largely on our current expectations and are subject to a number of risks and uncertainties. Actual results could differ materially from these forward-looking statements. Important factors to consider in evaluating such forward-looking statements include (i) changes in external factors or in our internal budgeting process which might impact trends in our results of operations; (ii) unanticipated working capital or other cash requirements; (iii) changes in our business strategy or an inability to execute our strategy due to unanticipated changes in the industries in which we operate; and (iv) various competitive market factors that may prevent us from competing successfully in the marketplace.

Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's opinions only as of the date hereof. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements.

**OVERVIEW**

The Singing Machine Company, Inc., a Delaware corporation, and its subsidiary (the "Singing Machine," "we," or "us") are primarily engaged in the design, marketing, and sale of consumer karaoke audio equipment, accessories, musical recordings and Bratz licensed electronic products. The Company's products are sold directly to distributors and retail customers. Our electronic karaoke machines and audio software products are marketed under The Singing Machine(R) and Motown trademarks.

Our products are sold throughout North America and Europe, primarily through department stores, lifestyle merchants, mass merchandisers, direct mail catalogs and showrooms, music and record stores, national chains, specialty stores and warehouse clubs.

Our karaoke machines and karaoke software are currently sold in such major retail outlets as Best Buy, Costco, Kohl's, J.C. Penney, Radio Shack, Wal-Mart and Sam's Club. Our Bratz products are sold in Toys R Us.

**RESULTS OF OPERATIONS**

The following table sets forth, for the periods indicated, certain items related to our consolidated statements of operations as a percentage of net revenues for the three months ended June 30, 2007 and 2006.

**The Singing Machine Company, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

	<b>For Three Months Ended</b>	
	<b>June 30, 2007</b>	<b>June 30, 2006</b>
<b>Net Sales</b>	100.0%	100.0%
<b>Cost of Goods Sold</b>	86.1%	87.8%
<b>Gross Profit</b>	13.9%	12.2%
<b>Operating Expenses</b>		
Selling expenses	6.7%	0.4%
General and administrative expenses	39.3%	112.5%
Depreciation and amortization	2.5%	10.4%
<b>Total Operating Expenses</b>	48.5%	123.3%
<b>Loss from Operations</b>	-34.6%	-111.1%
<b>Other Income (Expenses)</b>		
Other income	0.0%	0.9%
Interest expense	-0.2%	-0.9%
<b>Net Other Expenses</b>	-0.2%	0.0%

<b>Net Loss</b>	-34.8%	-111.1%
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**QUARTER ENDED JUNE 30, 2007 COMPARED TO THE QUARTER ENDED JUNE 30, 2006**

**NET SALES**

Net sales for the quarter ended June 30, 2007 increased to \$2,446,100 from \$1,035,876, an increase of \$1,410,224 as compared to the same period ended June 30, 2006. This increase can be primarily attributed to approximately \$550,000 of sales of Bratz products and an increase of sales to European customers of approximately \$500,000

**GROSS PROFIT**

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Our gross profit for the quarter ended June 30, 2007 increased to \$339,352 from \$126,472, an increase of \$212,880 as compared to the same period in the prior year. As a percentage of revenues, our gross profit for the three months ended June 30, 2007 increased to 13.9% from 12.2% for the same period in 2006. The increase of gross profit as a percentage of revenues was primarily due to less music returns, which yield higher profit margins, this quarter compared to the same period last year.

## **OPERATING EXPENSES**

For the three months ended June 30, 2007, total operating expenses decreased to \$1,186,379 from \$1,277,476 for the three months ended June 30, 2006, a decrease of \$91,097. Management has consistently reduced its operating expenses. This decrease of operating expenses is primarily due to the following factors:

- 1) Selling expense increased approximately \$160,000 which was primarily due to the increase of royalty expense for sales of licensed products as well as increased freight charges for a major customer.
- 2) General and administrative expenses decreased \$205,000 which was primarily due to the reduction of compensation expenses, legal expense and warehouse and office rental.

Our management will continue to implement cost cutting efforts in order to further reduce operating expenses for the remaining period of the current fiscal year.

## **OTHER INCOME/EXPENSES**

Our net other expenses increased to \$5,289 (interest expense) from \$84 for the same period a year ago.

## **INCOME TAXES**

For the three months ended June 30, 2007 and 2006, the Company did not record a tax provision because it expects sufficient future net losses to offset the income for these periods.

## **NET LOSS**

The net loss decreased to \$852,316 from a net loss of \$1,151,088 for the same period a year ago. The decrease of net loss was primarily due to the reduction of operating expenses and other expenses as described above as well as the increase in sales.

## **LIQUIDITY AND CAPITAL RESOURCES**

As of June 30, 2007, Singing Machine had cash on hand of \$1,003,071 as compared to cash on hand of \$168,635 as of June 30, 2006. We had working capital of \$2,208,514 as of June 30, 2007.

Net cash used by operating activities was \$427,878 for the three months ended June 30, 2007, as compared to \$1,467,929 used by operating activities the same period a year ago. The decrease of net cash used was a result of the following factors: operating loss, increase of receivables due to increased sales and higher inventory needed for the launch of the Bratz products. These increases were offset by the increase in the payable to the suppliers in Hong Kong.

Net cash used by investing activities for the three months ended June 30, 2007 was \$31,434 as compared to \$196,855 provided by investing activities for the same period ended a year ago. This increase was caused by the purchase of additional tooling this quarter.



Net cash provided by financing activities was \$273,483 for the three months ended June 30, 2007, as compared to \$1,016,162 for the same period ended a year ago. We received \$1 million from koncepts international as the final payment for the \$3 million equity investment in first quarter of fiscal 2007.

As of June 30, 2007, our unrestricted cash on hand was \$1,003,071. Our average monthly general and administrative expenses are approximately \$300,000. We expect that we will require approximately \$1 million for working capital during the next three-month period.

During the next 12 month period, we plan on financing our operation needs by:

- Raising additional working capital;
- Collecting our existing accounts receivable;
  - Selling existing inventory;
  - Vendor financing;
- Borrowing from factoring bank;
- Short term loans from the major investor.

Our sources of cash for working capital in the long term, 12 months and beyond, are the same as our sources during the short term. We are actively seeking additional financing facilities and capital investments to maintain and grow our business. If we need to obtain additional financing and fail to do so, it may have a material adverse effect on our ability to meet our financial obligations and to continue as a going concern.

Our commitments for debt and other contractual obligations as of June 30, 2007 are summarized as follows:

	Total	Less than 1 year	1 - 3 years	3 - 5 years	Over 5 years
Property Leases	\$ 476,165	\$ 464,343	\$ 11,822	\$ -	\$ -
Equipment Leases	32,316	9,888	22,428	-	-
Subordinated Debt - Related Party	225,000	225,000	-	-	-
Licensing Agreement	356,000	243,000	113,000	-	-
Interest Payments	-	-	-	-	-
<b>Total</b>	<b>\$ 1,089,481</b>	<b>\$ 942,231</b>	<b>\$ 147,250</b>	<b>\$ -</b>	<b>\$ -</b>

## INVENTORY SELL THROUGH

We monitor the inventory levels and sell through activity of our major customers to properly anticipate returns and maintain the appropriate level of inventory. We believe that we have proper return reserves to cover potential returns based on historical return ratios and information available from the customers.

## SEASONAL AND QUARTERLY RESULTS

Historically, our operations have been seasonal, with the highest net sales occurring in our fiscal second and third quarters (reflecting increased orders for equipment and music merchandise during the Christmas holiday season) and to a lesser extent the first and fourth quarters of the fiscal year. Sales in our fiscal second and third quarter, combined, accounted for approximately 94% and 87.5% of net sales in fiscal 2007 and 2006, respectively.

Our results of operations may also fluctuate from quarter to quarter as a result of the amount and timing of orders placed and shipped to customers, as well as other factors. The fulfillment of orders can therefore significantly affect results of operations on a quarter-to-quarter basis.

We are currently developing and considering selling products other than karaoke category during the slow season to fulfill the revenue shortfall.

## INFLATION

Inflation has not had a significant impact on The Singing Machine's operations. Singing Machine has historically passed any price increases on to its customers since prices charged by Singing Machine are generally not fixed by long-term contracts.

## OFF-BALANCE SHEET ARRANGEMENTS

We do not have any off balance sheet arrangements that are reasonably likely to have a current or future effect on our financial condition, revenues, results of operations, liquidity or capital expenditures.

## CRITICAL ACCOUNTING POLICIES

We prepared our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. As such, management is required to make certain estimates, judgments and assumptions that it believes are reasonable based on the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the periods presented. The significant accounting policies which management believes are the most

critical to aid in fully understanding and evaluating our reported financial results include: accounts receivable allowance for doubtful accounts, reserves on inventory, deferred tax assets and our Macau income tax exemption.

**COLLECTIBILITY OF ACCOUNTS RECEIVABLE.** The Singing Machine's allowance for doubtful accounts is based on management's estimates of the creditworthiness of its customers, current economic conditions and historical information, and, in the opinion of management, is believed to be an amount sufficient to respond to normal business conditions. Management sets 100% reserves for customers in bankruptcy and other reserves based upon historical collection experience. Should business conditions deteriorate or any major customer default on its obligations to the Company, this allowance may need to be significantly increased, which would have a negative impact on operations.

**RESERVES ON INVENTORIES.** The Singing Machine establishes a reserve on inventory based on the expected net realizable value of inventory on an item-by-item basis when it is apparent that the expected realizable value of an inventory item falls below its original cost. A charge to cost of sales results when the estimated net realizable value of specific inventory items declines below cost. Management regularly reviews the Company's investment in inventories for such declines in value.

**INCOME TAXES.** Significant management judgment is required in developing our provision for income taxes, including the determination of foreign tax liabilities, deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. Management evaluates its ability to realize its deferred tax assets on a quarterly basis and adjusts its valuation allowance when it believes that it is more likely than not that the asset will not be realized.

We operate within multiple taxing jurisdictions and are subject to audit in those jurisdictions. Because of the complex issues involved, any claims can require an extended period to resolve. In management's opinion, adequate provisions for potential income taxes in the jurisdiction have been made.

**OTHER ESTIMATES.** We make other estimates in the ordinary course of business relating to sales returns and allowances, warranty reserves, and reserves for promotional incentives. Historically, past changes to these estimates have not had a material impact on our financial condition. However, circumstances could change which may alter future expectations.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market risk represents the risk of loss that may impact our financial position, results of operations or cash flows due to adverse changes in financial and commodity market prices and rates. We are exposed to market risk in the areas of changes in United States and international borrowing rates and changes in foreign currency exchange rates. In addition, we are exposed to market risk in certain geographic areas that have experienced or remain vulnerable to an economic downturn, such as China. We purchase substantially our entire inventory from companies in China, and, therefore, we are subject to the risk that such suppliers will be unable to provide inventory at competitive prices. While we believe that, if such an event were to occur, we would be able to find alternative sources of inventory at competitive prices, we cannot assure you that we would be able to do so. These exposures are directly related to our normal operating and funding activities. Historically and as of June 30, 2007, we have not used derivative instruments or engaged in hedging activities to minimize market risk.

#### **INTEREST RATE RISK**

As of June 30, 2007, our exposure to market risk resulting from changes in interest rates is immaterial.

#### **FOREIGN CURRENCY RISK**

We have a wholly-owned subsidiary in Macau. Sales by this operation made on a FOB China or Hong Kong basis are dominated in U.S. dollars. However, purchases of inventory and Macau operating expenses are typically denominated in either Hong Kong dollars or the Macau currency ("MOP"), thereby creating exposure to changes in exchange rates. Changes in the Hong Kong dollar, U.S. dollar or MOP exchange rates may positively or negatively affect our gross margins, operating income and retained earnings. We do not believe that near-term changes in the exchange rates, if any, will result in a material effect on our future earnings, fair values or cash flows, and therefore, we have chosen not to enter into foreign currency hedging transactions. We cannot be assured that this approach will be successful, especially in the event of a significant and sudden change in the value of the MOP or Hong Kong dollar.

### **ITEM 4. CONTROLS AND PROCEDURES**

(a) ***Evaluation of Disclosure Controls and Procedures.*** As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based upon this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms and is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

(b) ***Changes in Internal Controls.*** There was no change in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 or 15d-15 under the Exchange Act that occurred during the end of the period covered by this report that has materially affected, or is reasonably likely to materially affect our internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

Not applicable.

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**ITEM 1A. RISK FACTORS**

**FACTORS THAT MAY AFFECT OUR FUTURE RESULTS AND THE MARKET PRICE OF OUR STOCK  
RISKS ASSOCIATED WITH OUR BUSINESS**

**WE ARE RELYING ON ONE FACTORING FACILITY TO FINANCE OUR ACCOUNTS RECEIVABLE. THE LOSS OF THIS ONE FACTORING FACILITY MAY CAUSE A PROBLEM FULFILLING CUSTOMER ORDERS RESULTING IN A LOSS OF REVENUES.**

The factoring facility at Crestmark Bank expired on August 1, 2007. We are currently working with a factoring company and a bank in Hong Kong to establish a new factoring facility. We expect to finalize the agreement within 30 days. However, there is no assurance that we will obtain a new facility. If we cannot obtain an additional banking facility, we may need to borrow a bridge loan or request that the factories extend their payment terms. If we fail to do so, we may not be able to fulfill customer orders.

**THE MUSIC INDUSTRY HAS BEEN EXPERIENCING A CONTINUED DECLINE OF COMPACT DISC (CD) SALES. OUR KARAOKE CD SALES COULD DECLINE FURTHER IN THE FUTURE.**

Due to the expansion of the music download business, the sales of Compact Discs (CD) have been declining in recent years. Our karaoke CD sales have been declining since 2004 and may continue to decline in the future. Music revenue accounts for approximately 3% of our total revenues.

**A SMALL NUMBER OF OUR CUSTOMERS ACCOUNT FOR A SUBSTANTIAL PORTION OF OUR REVENUES, AND THE LOSS OF ONE OR MORE OF THESE KEY CUSTOMERS COULD SIGNIFICANTLY REDUCE OUR REVENUES AND CASH FLOW.**

We rely on a few large customers to provide a substantial portion of our revenues. As a percentage of total revenues, our net sales to our five largest customers during the year ended March 31, 2007 and year ended March 31, 2006 were approximately 57% and 55%, respectively. We do not have long-term contractual arrangements with any of our customers and they can cancel their orders at any time prior to delivery. A substantial reduction in or termination of orders from any of our largest customers would decrease our revenues and cash flow.

**WE ARE RELYING ON ONE FACTORY TO MANUFACTURE AND PRODUCE THE MAJORITY OF OUR KARAOKE MACHINES FOR FISCAL 2008, AND IF THE RELATIONSHIP WITH THIS FACTORY IS DAMAGED OR INJURED IN ANY WAY, IT WOULD REDUCE OUR REVENUES AND PROFITABILITY.**

We have worked out a written agreement with a factory in China to produce most of our karaoke machines for fiscal 2008. If the factory is unwilling or unable to deliver our karaoke machines to us, our business will be adversely affected. Because our cash on hand is minimal, we are relying on revenues received from the sale of our ordered karaoke machines to provide cash flow for our operations. If we do not receive cash from these sales, we may not be able to continue our business operations.

**WE ARE RELYING ON ONE DISTRIBUTOR TO DISTRIBUTE OUR MUSIC PRODUCTS, IF THE DISTRIBUTION AGREEMENT IS TERMINATED, IT WOULD REDUCE OUR REVENUES AND PROFITABILITY.**

We are relying on Warner Elektra Atlantic Corporation (WEA) to distribute our music products in fiscal 2008, if the distribution agreement is terminated, our music revenues might decrease as well as our profitability.

**WE ARE SUBJECT TO THE RISK THAT SOME OF OUR LARGE CUSTOMERS MAY RETURN KARAOKE PRODUCTS THAT THEY HAVE PURCHASED FROM US AND IF THIS HAPPENS, IT WOULD REDUCE OUR REVENUES AND PROFITABILITY.**

In fiscal 2007 and 2006, a number of our customers and distributors returned karaoke products that they had purchased from us. Our customers returned goods valued at \$3.8 million or 14% of our net sales in fiscal 2007. Some of the returns resulted from customer's overstock of the products. Although we were not contractually obligated to accept return of the products, we accepted the returns because we value our relationship with our customers. Because we are dependent upon a few large customers, we are subject to the risk that any of these customers may elect to return unsold karaoke products to us in the future. If any of our customers were to return karaoke products to us, it would reduce our revenues and profitability.

**WE ARE SUBJECT TO PRESSURE FROM OUR CUSTOMERS RELATING TO PRICE REDUCTION AND FINANCIAL INCENTIVES AND IF WE ARE PRESSURED TO MAKE THESE CONCESSIONS TO OUR CUSTOMERS, IT WILL REDUCE OUR REVENUES AND PROFITABILITY.**

Because there is intense competition in the karaoke industry, we are subject to pricing pressure from our customers. Many of our customers have demanded that we lower our prices or they will buy our competitor's products. If we do not meet our customer's demands for lower prices, we will not sell as many karaoke products. In the fiscal year ended March 31, 2007, our sales to customers in the United States decreased because of increased price competition. We are also subject to pressure from our customers regarding certain financial incentives, such as return credits or large advertising or cooperative advertising allowances, which effectively reduce our profit. We gave advertising allowances of approximately \$200,000 during fiscal 2007 and fiscal 2006. We have historically offered advertising allowances to our customers because it is standard practice in the retail industry.

**WE EXPERIENCE DIFFICULTY FORECASTING THE DEMAND FOR OUR KARAOKE PRODUCTS AND IF WE DO NOT ACCURATELY FORECAST DEMAND, OUR REVENUES, NET INCOME AND CASH FLOW MAY BE AFFECTED.**

Because of our reliance on manufacturers in China for our machine production, our production lead times range from one to four months. Therefore, we must commit to production in advance of customers orders. It is difficult to forecast customer demand because we do not have any scientific or quantitative method to predict this demand. Our forecasting is based on management's general expectations about customer demand, the general strength of the retail market and management's historical experiences. We overestimated demand for our products in fiscal 2003 and 2004 and had \$5.9 million in inventory as of March 31, 2004. Because of this excess inventory, we had liquidity problems in fiscal 2005 and our revenues, net income and cash flow were adversely affected.

**WE ARE SUBJECT TO THE COSTS AND RISKS OF CARRYING INVENTORY FOR OUR CUSTOMERS AND IF WE HAVE TOO MUCH INVENTORY, IT WILL AFFECT OUR REVENUES AND NET INCOME.**

Many of our customers place orders with us several months prior to the holiday season, but they schedule delivery two or three weeks before the holiday season begins. As such, we are subject to the risks and costs of carrying inventory during the time period between the placement of the order and the delivery date, which reduces our cash flow. As of March 31, 2007 we had \$2.3 million in inventory on hand. It is important that we sell this inventory during fiscal 2008, so we have sufficient cash flow for operations.

**WE HAVE EXPERIENCED A SEVERE SHORTAGE OF A KEY COMPONENT, WHICH COULD DELAY OUR PRODUCT SCHEDULE AND NEGATIVELY IMPACT OUR PROFIT MARGIN.**

This year, there is a shortage of TFT LCD screens in the market. The screen is a key component of one of our new products. If we cannot secure enough quantity, we may not be able to delivery the product on time. This could result in order cancellations. In addition, the price increase of this component will have negative impact on our profit margin.

**OUR GROSS PROFIT MARGINS HAVE DECREASED OVER THE PAST YEAR AND WE EXPECT A COMPETITIVE MARKET.**

Over the past year, our gross profit margins have generally decreased due to the competition except for fiscal 2005 when we had developed several new models, which were in demand and yielded higher profit margins. We expect that our gross profit margin might decrease under downward pressure in fiscal 2008.

**OUR BUSINESS IS SEASONAL AND THEREFORE OUR ANNUAL OPERATING RESULTS WILL DEPEND, IN LARGE PART, ON OUR SALES DURING THE RELATIVELY BRIEF HOLIDAY SEASON.**

Sales of consumer electronics and toy products in the retail channel are highly seasonal, with a majority of retail sales occurring during the period from September through December in anticipation of the holiday season, which includes Christmas. A substantial majority of our sales occur during the second quarter ending September 30 and the third quarter ending December 31. Sales in our second and third quarter, combined, accounted for approximately 94.0%, 87.5% and 86.7% of net sales in fiscal 2007, 2006 and 2005, respectively.

**IF WE ARE UNABLE TO COMPETE IN THE KARAOKE PRODUCTS CATEGORY, OUR REVENUES AND NET PROFITABILITY WILL BE REDUCED.**

Our major competitors for karaoke machines and related products are Memorex and GPX. We believe that competition for karaoke machines is based primarily on price, product features, reputation, delivery times, and



customer support. Our primary competitors for producing karaoke music are Compass, Pocket Songs, Sybersound, UAV and Sound Choice. We believe that competition for karaoke music is based primarily on popularity of song titles, price, reputation, and delivery times. To the extent that we lower prices to attempt to enhance or retain market share, we may adversely impact our operating margins. Conversely, if we opt not to match competitor's price reductions we may lose market share, resulting in decreased volume and revenue. To the extent our leading competitors reduce prices on their karaoke machines and music; we must remain flexible to reduce our prices. If we are forced to reduce our prices, it will result in lower margins and reduced profitability. Because of intense competition in the karaoke industry in the United States during fiscal 2007, we expect that the intense pricing pressure in the low end of the market will continue in the karaoke market in the United States in fiscal 2008. In addition, we must compete with all the other existing forms of entertainment including, but not limited to: motion pictures, video arcade games, home video games, theme parks, nightclubs, television, prerecorded tapes, CD's, and video cassettes.

**IF WE ARE UNABLE TO DEVELOP NEW KARAOKE PRODUCTS, OUR REVENUES MAY NOT CONTINUE TO GROW.**

The karaoke industry is characterized by rapid technological change, frequent new product introductions and enhancements and ongoing customer demands for greater performance. In addition, the average selling price of any karaoke machine has historically decreased over its life, and we expect that trend to continue. As a result, our products may not be competitive if we fail to introduce new products or product enhancements that meet evolving customer demands. The development of new products is complex, and we may not be able to complete development in a timely manner. To introduce products on a timely basis, we must:

- accurately define and design new products to meet market needs;
- design features that continue to differentiate our products from those of our competitors;
  - transition our products to new manufacturing process technologies;
  - identify emerging technological trends in our target markets;
- anticipate changes in end-user preferences with respect to our customers' products;
- bring products to market on a timely basis at competitive prices; and
- respond effectively to technological changes or product announcements by others.

We believe that we will need to continue to enhance our karaoke machines and develop new machines to keep pace with competitive and technological developments and to achieve market acceptance for our products. At the same time, we need to identify and develop other products which may be different from karaoke machines.

**OUR PRODUCTS ARE SHIPPED FROM CHINA AND ANY DISRUPTION OF SHIPPING COULD PREVENT OR DELAY OUR CUSTOMERS' RECEIPT OF INVENTORY.**

We rely principally on four contract ocean carriers to ship virtually all of the products that we import to our warehouse facility in Compton, California. Retailers that take delivery of our products in China rely on a variety of carriers to import those products. Any disruptions in shipping, whether in California or China, caused by labor strikes, other labor disputes, terrorism, and international incidents may prevent or delay our customers' receipt of inventory. If our customers do not receive their inventory on a timely basis, they may cancel their orders or return products to us. Consequently, our revenues and net income would be reduced.

**OUR MANUFACTURING OPERATIONS ARE LOCATED IN THE PEOPLE'S REPUBLIC OF CHINA, SUBJECTING US TO RISKS COMMON IN INTERNATIONAL OPERATIONS. IF THERE IS ANY PROBLEM WITH THE MANUFACTURING PROCESS, OUR REVENUES AND NET PROFITABILITY MAY BE REDUCED.**

We are using eight factories in the People's Republic of China to manufacture the majority of our karaoke machines. These factories will be producing nearly all of our karaoke products in fiscal 2008. Our arrangements with these factories are subject to the risks of doing business abroad, such as import duties, trade restrictions, work stoppages, and foreign currency fluctuations, limitations on the repatriation of earnings and political instability, which could have an adverse impact on our business. Furthermore, we have limited control over the manufacturing processes. As a result, any difficulties encountered by our third-party manufacturers that result in product defects, production delays, cost overruns or the inability to fulfill orders on a timely basis could adversely affect our revenues, profitability and cash flow. Also, since we do not have written agreements with any of these factories, we are subject to additional uncertainty if the factories do not deliver products to us on a timely basis.

**WE DEPEND ON THIRD PARTY SUPPLIERS FOR PARTS FOR OUR KARAOKE MACHINES AND RELATED PRODUCTS, AND IF WE CANNOT OBTAIN SUPPLIES AS NEEDED, OUR OPERATIONS WILL BE SEVERELY DAMAGED.**

Our growth and ability to meet customer demand depends in part on our capability to obtain timely deliveries of karaoke machines and our electronic products. We rely on third party suppliers to produce the parts and materials we use to manufacture and produce these products. If our suppliers are unable to provide our factories with the parts and

supplies, we will be unable to produce our products. We cannot guarantee that we will be able to purchase the parts we need at reasonable prices or in a timely fashion. In the last several years, there have been shortages of certain chips that we use in our karaoke machines. If we are unable to anticipate any shortages of parts and materials in the future, we may experience severe production problems, which would impact our sales.

**CONSUMER DISCRETIONARY SPENDING MAY AFFECT KARAOKE PURCHASES AND IS AFFECTED BY VARIOUS ECONOMIC CONDITIONS AND CHANGES.**

Our business and financial performance may be damaged more than most companies by adverse financial conditions affecting our business or by a general weakening of the economy. Purchases of karaoke machines and music are considered discretionary for consumers. Our success will therefore be influenced by a number of economic factors affecting discretionary and consumer spending, such as employment levels, business, interest rates, and taxation rates, all of which are not under our control. Additionally, other extraordinary events such as terrorist attacks or military engagements, which adversely affect the retail environment may restrict consumer spending and thereby adversely affect our sales growth and profitability.

**WE MAY HAVE INFRINGED THE COPYRIGHTS OF CERTAIN MUSIC PUBLISHERS AND IF WE VIOLATE FEDERAL COPYRIGHT LAWS, WE WILL BE SUBJECT TO MONETARY PENALTIES.**

Over the past several years, the Singing Machine (like its competitors) has received notices from certain music publishers alleging that the full range of necessary rights in their copyrighted works has not been properly licensed in order to sell those works as part of products known as “compact discs with graphics” (“CDG”s). CDG's are compact discs which contain the musical recordings of karaoke songs and graphics which contain the lyrics of the songs. Singing Machine has negotiated licenses with the complaining parties, or is in the process of settling such claims, with each one of the complaining copyright owners. As with any alleged copyright violations, unlicensed users may be subject to damages under the U.S. Copyright Act. Such damages and claims could have a negative effect on Singing Machine’s ability to sell its music products to its customers. This is the reason the Singing Machine pursues licenses so diligently.

**WE MAY BE SUBJECT TO CLAIMS FROM THIRD PARTIES FOR UNAUTHORIZED USE OF THEIR PROPRIETARY TECHNOLOGY, COPYRIGHTS OR TRADE SECRETS AND ANY CLAIMS ASSERTED AGAINST US COULD AFFECT OUR NET PROFITABILITY.**

We believe that we independently developed the technology used in our electronic and audio software products and that it does not infringe on the proprietary rights, copyrights or trade secrets of others. However, we cannot be sure that we have not infringed on the proprietary rights of third parties or those third parties will not make infringement violation claims against us. During fiscal 2000, Tanashin Denki, Ltd., a Japanese company that holds a patent on a cassette tape drive mechanism alleged that some of our karaoke machines violated their patents. We settled the matters with Tanashin in December 1999. Subsequently in December 2002, Tanashin again alleged that some of our karaoke machines violated their patents. We entered into another settlement agreement with them in May 2003. In addition to Tanashin, we could receive infringement claims from other third parties. Any infringement claims may have a negative effect on our profitability and financial condition.

**WE ARE EXPOSED TO THE CREDIT RISK OF OUR CUSTOMERS, WHO ARE EXPERIENCING FINANCIAL DIFFICULTIES, AND IF THESE CUSTOMERS ARE UNABLE TO PAY US, OUR REVENUES AND PROFITABILITY WILL BE REDUCED.**

We sell products to retailers, including department stores, lifestyle merchants, direct mail catalogs and showrooms, national chains, specialty stores, and warehouse clubs. Some of these retailers, such as K-Mart, FAO Schwarz and KB Toys, have engaged in leveraged buyouts or transactions in which they incurred a significant amount of debt, and operated under the protection of bankruptcy laws. As of August 8, 2007 we are aware of only three customers, FAO Schwarz, Musicland, and KB Toys, which are operating under the protection of bankruptcy laws. Deterioration in the financial condition of our customers could result in bad debt expense to us and have a material adverse effect on our revenues and future profitability.

**A DISRUPTION IN THE OPERATION OF OUR WAREHOUSE CENTERS IN CALIFORNIA OR FLORIDA COULD IMPACT OUR ABILITY TO DELIVER MERCHANDISE TO OUR CUSTOMERS, WHICH COULD ADVERSELY AFFECT OUR REVENUES AND PROFITABILITY.**

A significant amount of our merchandise is shipped to our customers from one of our two warehouses, which are located in Compton, California, and Coconut Creek, Florida. Events such as fire or other catastrophic events, any malfunction or disruption of our centralized information systems or shipping problems may result in delays or disruptions in the timely distribution of merchandise to our customers, which could substantially decrease our revenues and profitability.

**OUR BUSINESS OPERATIONS COULD BE DISRUPTED IF THERE ARE LABOR PROBLEMS ON THE WEST COAST.**

During fiscal 2007, approximately 40% of our sales were domestic warehouse sales, which were made from our warehouses in California and Florida. During the third quarter of fiscal 2003, the dock strike on the West Coast affected sales of two of our karaoke products and we estimate that we lost between \$3 and \$5 million in orders because we could not get the containers of these products off the pier. If another strike or work slow-down occurs and we do not have a sufficient level of inventory, a strike or work slow-down would result in increased costs to us and may reduce our profitability.

**CURRENCY EXCHANGE RATE RISK**

Our major suppliers are located in China. The Chinese local currency has depreciated approximately 5% against the US dollar in 2007. If this trend continues, our costs may increase in the future. This may decrease our profit margin.

**RISKS ASSOCIATED WITH OUR CAPITAL STRUCTURE**

**THE MARKET PRICE OF OUR COMMON STOCK MAY BE VOLATILE WHICH MAY CAUSE INVESTORS TO LOSE ALL OR A PORTION OF THEIR INVESTMENT.**

From December 1, 2004 through June 30, 2007, our common stock has traded between a high of \$1.60 and a low of \$0.21. During this period, we had liquidity problems and incurred a net loss of \$1.9 million in fiscal 2006 and loss of \$3.6 million in fiscal 2005. Our stock price may continue to be volatile based on similar or other adverse developments in our business. In addition, the stock market periodically experiences significant adverse price and volume fluctuations which may be unrelated to the operating performance of particular companies.

**IF INVESTORS SHORT OUR SECURITIES, IT MAY CAUSE OUR STOCK PRICE TO DECLINE.**

During the past year, a number of investors have held a short position in our common stock. As of July 10, 2007, investors held a short position of approximately 36,110 shares of our common stock which represented 0.10% of our public float. The anticipated downward pressure on our stock price due to actual or anticipated sales of our stock by some institutions or individuals who engage in short sales of our common stock could cause our stock price to decline. Additionally, if our stock price declines, it may be more difficult for us to raise capital.

**OUR COMMON STOCK MAY BE DELISTED FROM THE AMERICAN STOCK EXCHANGE, WHICH MAY HAVE A MATERIAL ADVERSE IMPACT ON THE PRICING AND TRADING OF OUR COMMON STOCK.**

On September 6, 2006, the Company received notice from The American Stock Exchange (the "Amex") that the Company has fallen below the continued listing standards of the Amex and that its listing is being continued pursuant to an extension.

Specifically, for the fiscal years ended March 31, 2007 and March 31, 2006, the Company was not in compliance with Section 1003(a)(ii) of the Amex Company Guide with shareholders' equity of less than \$4,000,000 and net losses in three of its four most recent fiscal years.

The Company was previously added to the list of issuers that are not in compliance with the Amex's continued listing standards, and the Company's trading symbol SMD remains subject to the extension .BC to denote its noncompliance. This indicator will remain in effect until such time as the Company has regained compliance with all applicable continued listing standards.

If our common stock is removed from listing on Amex, it may become more difficult for us to raise funds through the sales of our common stock or securities.

**IF OUR OUTSTANDING DERIVATIVE SECURITIES ARE EXERCISED OR CONVERTED, OUR EXISTING SHAREHOLDERS WILL SUFFER DILUTION.**

As of June 30, 2007, there were outstanding stock options to purchase an aggregate of 1,240,375 shares of common stock at exercise prices ranging from \$.32 to \$11.09 per share, not all of which are immediately exercisable. The weighted average exercise price of the outstanding stock options is approximately \$1.35 per share. As of June 30, 2007, there were outstanding and immediately exercisable options to purchase an aggregate of 1,038,858 shares of our common stock. There were outstanding stock warrants to purchase 2,500,000 shares of common stock at exercise prices ranging from \$.28 to \$.35 per share, all of which are exercisable. The weighted average exercise price of the outstanding stock warrants is approximately \$0.315 per share.

**FUTURE SALES OF OUR COMMON STOCK HELD BY CURRENT STOCKHOLDERS AND INVESTORS MAY DEPRESS OUR STOCK PRICE.**

As of August 8, 2007 there were 29,898,876 shares of our common stock outstanding. We have filed two registration statements registering an aggregate 3,794,250 of shares of our common stock (a registration statement on Form S-8 to register the sale of 1,844,250 shares underlying options granted under our 1994 Stock Option Plan and a registration statement on Form S-8 to register 1,950,000 shares of our common stock underlying options granted under our Year 2001 Stock Option Plan). An additional registration statement on Form S-1 was filed in October 2003, registering an aggregate of 2,795,465 shares of our common stock. The market price of our common stock could drop due to the sale of large number of shares of our common stock, such as the shares sold pursuant to the registration statements or under Rule 144, or the perception that these sales could occur.

**OUR STOCK PRICE MAY DECREASE IF WE ISSUE ADDITIONAL SHARES OF OUR COMMON STOCK.**

Our Certificate of Incorporation authorizes the issuance of 100,000,000 shares of common stock as amended in January 2006. As of August 8, 2007 we had 29,898,876 shares of common stock issued and outstanding and an aggregate of 3,740,375 shares issuable under our outstanding options and warrants. As such, our Board of Directors has the power, without stockholder approval, to issue up to 66,360,749 shares of common stock.

Any issuance of additional shares of common stock, whether by us to new stockholders or the exercise of outstanding warrants or options, may result in a reduction of the book value or market price of our outstanding common stock. Issuance of additional shares will reduce the proportionate ownership and voting power of our then existing stockholders.

**PROVISIONS IN OUR CHARTER DOCUMENTS AND DELAWARE LAW MAKE IT DIFFICULT FOR A THIRD PARTY TO ACQUIRE OUR COMPANY AND COULD DEPRESS THE PRICE OF OUR COMMON STOCK.**

Delaware law and our certificate of incorporation and bylaws contain provisions that could delay, defer or prevent a change in control of our Company or a change in our management. These provisions could also discourage proxy contests and make it more difficult for you and other stockholders to elect directors and take other corporate actions. These provisions of our restated certificate of incorporation include: authorizing our board of directors to issue additional preferred stock, limiting the persons who may call special meetings of stockholders, and establishing advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted on by stockholders at stockholder meetings.

**IF WE FAIL TO MAINTAIN EFFECTIVE INTERNAL CONTROLS OVER FINANCIAL REPORTING, THE PRICE OF OUR COMMON STOCK MAY BE ADVERSELY AFFECTED.**

Our internal controls over financial reporting may have weaknesses and conditions that need to be addressed, the disclosure of which may have an adverse impact on the price of our common stock. We are required to establish and maintain appropriate internal controls over financial reporting. Failure to establish those controls, or any failure of those controls once established, could adversely impact our public disclosures regarding our business, financial condition or results of operations. In addition, our management's assessment of internal controls over financial reporting may identify weaknesses and conditions that need to be addressed in our internal controls over financial reporting or other matters that may raise concerns for investors. Any actual or perceived weaknesses and conditions that need to be addressed in our internal controls over financial reporting, disclosure of our management's assessment of our internal controls over financial reporting or disclosure of our public accounting firm's attestation to or report on management's assessment of the Company's internal controls over financial reporting may have an adverse impact on the price of our common stock. Management will have to assess internal controls in accordance with Section 404 of the Sarbanes-Oxley Act for the fiscal year ending March 31, 2008.

**THE MARKET PRICE OF OUR COMMON STOCK MAY BE ADVERSELY AFFECTED BY SEVERAL FACTORS.**

The market price of our common stock could fluctuate significantly in response to various factors and events, including:

- our ability to execute our business plan;
- operating results below expectations;
- loss of any strategic relationship;
- industry developments;
- economic and other external factors; and
- period-to-period fluctuations in its financial results.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our common stock.

**WE HAVE NOT PAID CASH DIVIDENDS IN THE PAST AND DO NOT EXPECT TO PAY CASH DIVIDENDS IN THE FUTURE. ANY RETURN ON INVESTMENT MAY BE LIMITED TO THE VALUE OF OUR STOCK.**

We have never paid cash dividends on our stock and do not anticipate paying cash dividends on our stock in the foreseeable future. The payment of cash dividends on our stock will depend on our earnings, financial condition and other business and economic factors affecting us at such time as the board of directors may consider relevant. If we do not pay cash dividends, our stock may be less valuable because a return on your investment will only occur if our stock price appreciates.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**



\*None

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

We are not currently in default upon any of our senior securities.

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

Not applicable.

**ITEM 5. OTHER INFORMATION**

Not applicable

**ITEM 6. EXHIBITS**

31.1 Certification of Anton Handal, Chief Executive Officer, dated August 14, 2007, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.\*

31.2 Certification of Danny Zheng, Chief Financial Officer, dated August 14, 2007, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.\*

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32.1 Certifying Statement of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act.\*

32.2 Certifying Statement of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act.\*

\* Filed herewith

### **SIGNATURES**

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

**THE SINGING MACHINE COMPANY, INC.**

Date: August 14, 2007

By: */s/ Anton H. Handal*

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Anton H. Handal  
Chief Executive Officer