SINGING MACHINE CO INC
Form 10-Q/A
March 19, 2004

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-QSB/A

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

For the quarterly period ended December 31, 2001

0 - 24968

Commission File Number

THE SINGING MACHINE COMPANY, INC.

(Exact Name of Small Business Issuer as Specified in its Charter)

Delaware	95-3795478
(State of Incorporation)	(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)

Check whether the Issuer: (1) filed all reports required to be filed by section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements for the past 90 days. Yes x No

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes x No

APPLICABLE ONLY TO CORPORATE ISSUERS

There were 5,041,320 shares of Common Stock, $.01 par value, issued and outstanding at December 31, 2001.

THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY

EXPLANATORY NOTE

This Amendment No. 1 on Form 10-QSB/A filed by The Singing Machine Company, Inc. (the "Company") amends the Company's Quarterly Report on Form 10-QSB for the quarterly period ended December 31, 2001.

Subsequent to the filing of such Quarterly Report, Management made the decision to restate our quarterly financial statements for the quarter ended December 31, 2001 to include a provision for income tax expense relating to International SMC (HK) Limited, our Hong Kong subsidiary. In the Form 10-QSB that we previously filed for this quarter, we do not include a provision for this income tax, because we believed that International SMC `s offshore tax exemption would be approved.

In April 2001, International SMC applied for an offshore tax exemption, based on the locality of profits of the Hong Kong subsidiary. Management believed that the exemption would be approved because the source of all profits of the Hong Kong subsidiary is from exporting to customers outside of Hong Kong. Accordingly, no provision for income taxes was provided in quarterly report for the quarter ended December 31, 2001. Management is continuing its exemption application process. However, due to the extended period of time that the application has been outstanding, as well as management's reassessment of the probability that the application will be approved, management determined to restate the fiscal year 2002 and 2001 consolidated financial statements and certain related quarterly financial statements for fiscal 2002 and 2003 to provide for such taxes.

With regard to United States taxation of foreign income, the Company had originally taken the position that the foreign income of the Hong Kong subsidiary qualified for a deferral under the Internal Revenue Code allowing for such income to be indefinitely deferred and not taxed in the United States until such income is repatriated. Full disclosure of the amount and nature of the indefinite deferral for fiscal year 2002 was reflected in the income tax footnote of the consolidated financial statements for that year. The Internal Revenue Code, regulations and case law regarding international income taxation is quite complex and subject to interpretation. Each case is determined based on the individual facts and circumstances. Due to certain inter-company loans made in 2002 and 2003, the profits previously considered to be indefinitely deferred became partially taxable as "deemed dividends" under section 956 of the Internal Revenue Code. Although certain arguments against the imposition of a "deemed dividend" may be asserted, management has determined to restate the fiscal year 2002 consolidated financial statements based on its reassessment of its original position. The effect of such restatement is to increase income tax expense by $1,027,545 in fiscal year 2002, which includes the utilization of the foreign tax credits referred to above.

The net effect of the above two adjustments is to decrease net income by $1,286,119 for the quarter ended December 31, 2001 and $1,874,741 for the nine months then ended. The net effect on net income per share is to decrease net income per share basic and diluted by $0.41 and $0.36, respectively for the nine months ended December 31, 2001, and decrease net income per share basic and diluted by $0.26 and $0.23, respectively for the quarter ended December 31, 2001.

THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY

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THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY
PART I - FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

	December 31,	March 31,

	2001	2001
	(unaudited) (restated)	(restated)
ASSETS		
CURRENT ASSETS:		
Cash	$ 1,916,705	$ 1,016,221
Accounts Receivable, net of allowance of $9,812	27,059,905	955,652
Due from Factor	--	933,407
Due from Vendor	--	699,096
Inventories	6,713,553	4,813,461
Interest Receivable	--	7,425
Prepaid Expenses and Other Current Assets	479,498	598,487
TOTAL CURRENT ASSETS	36,169,660	9,023,749
PROPERTY AND EQUIPMENT, NET	648,280	263,791
OTHER ASSETS:		
Deposit for Credit Line	256,807	--
Due from related party	--	7,692
Due from officers	--	110,000
Investment in/advances to Unconsolidated Subsidiary	100,028	374,730
Reorganization Intangible - net	134,749	277,047
Deferred tax asset	526,247	452,673
TOTAL ASSETS	$37,835,772	$ 10,509,682
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts Payable	7,049,514	821,684
Accrued Expenses	4,230,376	746,017
Income taxes payable	2,343,165	491,744
Loan Payable	7,567,111	--
Notes Payable	--	--
Due to related party	673,113	--
TOTAL CURRENT LIABILITIES	21,863,279	2,059,445
STOCKHOLDERS' EQUITY:		
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 authorized, no shares issued and outstanding	--	--
Common Stock, $.01 par value; 18,900,000 shares authorized; 5,041,320 and 4,359,120 shares issued and outstanding, respectively	50,414	43,590
Additional Paid In Capital	4,274,033	3,324,779
Deferred Guarantee Fees	--	(171,472)
Retained Earnings	11,648,046	5,253,340

TOTAL STOCKHOLDERS' EQUITY	15,972,493	8,450,237
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$37,835,772	$ 10,509,682

See accompanying notes to consolidated financial statements

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THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended		Nine Months
	December 31, 2001	December 31, 2000	December 31, 2001
	(restated)		(restated)
NET SALES	$ 34,158,513	$ 13,863,790	$ 55,431,595
COST OF SALES	22,719,929	9,173,854	36,821,615
GROSS PROFIT	11,438,583	4,689,936	18,609,980
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	5,422,298	2,259,606	10,415,804
INCOME FROM OPERATIONS	6,016,286	2,430,330	8,194,176
OTHER INCOME (EXPENSES):			
Other income	53,600	10,268	195,741
Interest expense	(104,877)	(201,294)	(143,034)
Interest income	17,471	6,594	40,391
Factoring fees	--	(144,245)	173
NET OTHER EXPENSES	(33,806)	(328,677)	93,271
INCOME BEFORE INCOME TAX EXPENSE	5,982,480	2,101,653	8,287,447
INCOME TAX EXPENSE	1,292,119	371,522	1,892,741
NET INCOME	$ 4,690,361	$ 1,730,131	$ 6,394,706
NET INCOME PER COMMON SHARE			
Basic	$ 0.96	$ 0.40	$ 1.39
Diluted	$ 0.82	$ 0.34	$ 1.20

	============	============	============
WEIGHTED AVERAGE COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING			
Basic	4,890,505	4,360,772	4,600,612
Diluted	5,710,737	5,124,436	5,310,051

See accompanying notes to financial statements.

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THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended	
	December 31, 2001 (restated)	December 31, 2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$ 6,394,706	$ 3,386,465
Adjustments to reconcile net income to net cash provided by (used in) operating activities		
Depreciation and amortization	278,058	63,603
Stock based expenses	171,472	171,472
Changes in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	(26,104,253)	(4,236,963)
Due to(from) related party/vendor	1,372,209	394,706
Inventory	(1,900,092)	(1,076,428)
Prepaid expenses and other assets	118,989	(270,560)
Increase (decrease) in:		
Accounts payable and accrued expenses	9,712,189	3,586,190
Income taxes payable	1,851,421	--
Net Cash Provided by (Used in) Operating Activities	(8,105,301)	2,018,485
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(593,823)	(255,007)
Proceeds from factor	933,407	(2,510,158)
Proceeds from Officer	117,425	--
Deposit for Credit line	(256,807)	--
Investment/Advances in unconsolidated subsidiary	274,702	--
Due from related parties	7,692	(5,559)
Net Cash Provided by (Used in) Investing Activities	482,596	(2,770,724)
CASH FLOW FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock & exercise of warrants and options	956,078	580,645
Line of credit net proceeds	7,567,111	--
Net proceeds from notes payable	--	203,930

Net Cash Provided by (Used in) Financing Activities	8,523,189	784,575
Increase in cash and cash equivalents	900,484	32,336
Cash and cash equivalents - beginning of period	1,016,221	378,848
CASH AND CASH EQUIVALENTS - END OF PERIOD	$ 1,916,705	$ 411,184
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for interest	$ 143,034	$ 404,486
Cash paid during the year for income taxes	$ 18,000	$ 11,994

See accompanying notes to consolidated financial statements.

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THE SINGING MACHINE COMPANY, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2001

(Unaudited)

RESTATEMENT OF PREVIOUSLY REPORTED FINANCIAL STATEMENTS

Subsequent to the filing of this quarterly report, management made the decision to restate quarterly financial statements for the quarter ended December 31, 2001 to include a provision for income tax expense relating to International SMC (HK) Limited, the Hong Kong subsidiary. In the Form 10-QSB that was previously filed for this quarter, we did not include a provision for this income tax, because we believed that International SMC `s offshore tax exemption would be approved.

In April 2001, International SMC applied for an offshore tax exemption, based on the locality of profits of the Hong Kong subsidiary. Management believed that the exemption would be approved because the source of all profits of the Hong Kong subsidiary is from exporting to customers outside of Hong Kong. Accordingly, no provision for income taxes was provided in quarterly report for the quarter ended December 31, 2001. Management is continuing its exemption application process. However, due to the extended period of time that the application has been outstanding, as well as management's reassessment of the probability that the application will be approved, management determined to restate the fiscal year 2002 and 2001 consolidated financial statements and certain related quarterly financial statements for fiscal 2002 and 2003 to provide for such taxes.

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NOTE 1 - BASIS OF PRESENTATION

The accompanying consolidated financial statements of the Company have been prepared in accordance with the instructions to Form 10-QSB and, therefore, omit or condense certain footnotes and other information normally included in financial statements prepared in accordance with generally accepted accounting principles. It is suggested that these consolidated condensed financial statements should be read in conjunction with the Company's financial statements and notes thereto included in the Company's audited financial statements on Form 10-KSB for the fiscal year ended March 31, 2001.

The accounting policies followed for interim financial reporting are the same as those disclosed in Note 1 of the Notes to Financial Statements included in the Company's audited financial statements for the fiscal year ended March 31, 2001, which are included in Form 10- KSB.

The Financial Accounting Standards Board has recently issued several new accounting pronouncements which may apply to the Company. Statement No. 141 Business Combinations (SFAS 141) establishes revised standards for accounting for business combinations. Specifically, the statement eliminates the pooling method, provides new guidance for recognizing intangible assets arising in a business combination, and calls for disclosure of considerably more information about a business combination. This statement is effective for business combinations initiated on or after July 1, 2001. The adoption of this pronouncement on July 1, 2001 did not have a material effect on the Company's financial position, results of operations or liquidity. Statement No. 142 Goodwill and Other Intangible Assets (SFAS 142) provides new guidance concerning the accounting for the acquisition of intangibles, except those acquired in a business combination, which is subject to SFAS 141, and the manner in which intangibles and goodwill should be accounting for subsequent to their initial recognition. Generally, intangible assets with indefinite lives, and goodwill, are no longer amortized; they are carried at lower of cost or market and subject to annual impairment evaluation, or interim impairment evaluation if an interim triggering event occurs, using a new fair market value method. Intangible assets with finite lives are amortized over those lives, with no stipulated maximum, and an impairment test is performed only when a triggering event occurs. This statement is effective for all fiscal years beginning after December 15, 2001. The Company believes that the future implementation of SFAS 142 on April 1, 2002 will not have a material effect on the Company's financial position, results of operations or liquidity. Statement No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets supercedes Statement No. 121 Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of (SFAS 121). Though it retains the basic requirements of SFAS 121 regarding when and how to measure an impairment loss, SFAS 144 provides additional implementation guidance. SFAS 144 excludes goodwill and intangibles not being amortized among other exclusions. SFAS 144 also supercedes the provisions of APB 30, Reporting the Results of Operations, pertaining to discontinued operations. Separate reporting of a discontinued operation is still required, but SFAS 144 expands the presentation to include a component of an entity, rather than strictly a business segment as defined in SFAS 131, Disclosures about Segments of an Enterprise and Related Information. SFAS 144 also eliminates the current exemption to consolidation when control over a subsidiary is likely to be temporary. This statement is effective for all fiscal years beginning after December 15, 2001. The Company believes that the future implementation of SFAS 144 on April 1, 2002 will not have a material effect on the Company's financial position, results of operations or liquidity.

Certain amounts in the December 31, 2000 interim consolidated financial statements have been reclassified to conform to the December 31, 2001 presentation.

In the opinion of management, all adjustments which are of a normal recurring nature and considered necessary to present fairly the financial positions, results of operations, and cash flows for all periods presented have been made.

The results of operations for the nine month period ended December 31, 2001 are not necessarily indicative of the results that may be expected for the entire fiscal year ending March 31, 2002.

The accompanying consolidated condensed financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant inter-company balances and transactions have been eliminated. Assets and liabilities of the foreign subsidiary are translated at the rate of exchange in effect at the balance sheet date; income and expenses are translated at the average rates of exchange prevailing during the year. The related translation adjustment is not material.

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NOTE 2 - INVESTMENT IN AND ADVANCES TO UNCONSOLIDATED SUBSIDIARY

In November 2000, the Company closed on an acquisition of 60% of the ordinary voting shares of a Hong Kong toy company for a total purchase price of $170,000. The Company believed that the acquiree had agreed to extend the effective date to June 2001, but a dispute arose and the Company committed to dispose of the entire investment. Accordingly, pursuant to Statement of Financial Accounting Standards No. 94 Consolidation of All Majority-Owned Subsidiaries, the Company treated the control of the subsidiary as temporary and recorded the investment of $170,000 and advances and interest of $213,947 at cost.

The Company completed a contract selling the 60% interest on September 11, 2001. The transaction resulted in a net loss on investment of $48,912. The purchaser took over operation of the company on September 12, 2001. Payment of the remaining contract price, $90,002, took place over a four month period of time ending December 31, 2001. The advances and interest remaining at December 31, 2001, in the amount of $ 100,028, will be paid in full over a seven month period and will accrue additional interest over that time.

NOTE 3 - DEPOSIT FOR CREDIT LINE

The Company, through its Hong Kong subsidiary, is negotiating with a major international bank for credit facilities. Pursuant to these negotiations, the Company's subsidiary is required to maintain a separate depository account in the amount of $256,807.

NOTE 4 - LOANS AND LETTERS OF CREDIT

On May 19, 1999, as amended on February 14, 2000, the Company, through its Hong Kong Subsidiary, obtained a credit facility of $500,000 from a Hong Kong subsidiary of a Belgian bank. This facility is a revolving line of credit based upon drawing down a maximum of 15% of the value of export letters of credit lodged with Belgian Bank. There is no expiration date to this agreement, except that Belgian Bank reserves the right to revise the terms and conditions at the Bank's discretion. The cost of this credit facility is the U.S. Dollar prime rate plus 1.25%. Repayment of principal plus interest shall be made upon negotiation of the export letters of credit, but not later than 90-days after the advance. As of December 31, 2001, there was no outstanding balance on this credit facility.

On April 26, 2001, the Company executed a Loan and Security Agreement (the Agreement) with a commercial lender (the Lender). The Lender will advance up to 75% of the Company's eligible accounts receivable, plus up to 40% of the eligible inventory, plus up to 40% of the commercial letters of credit opened for the purchase of eligible inventory, less reserves of up to $1,200,000 as defined in the agreement.

The outstanding loan limit varies between zero and $10,000,000 depending on the time of year, as stipulated in the Agreement. The Lender will also issue or co-sign for commercial letters of credit up to $2,500,000, which shall reduce the loan limits above. The loans bear interest at the commercial lender's prime rate plus 0.5% and an annual fee equal to 1% of the maximum loan amount or $100,000 is payable. The term of the loan facility expires on April 26, 2004 and is automatically renewable for one-year terms. All amounts under the loan facility are due within 90 days of demand. The loans are secured by a first lien on all present and future assets of the Company except for certain tooling located at a vendor in China.

The Agreement contains a financial covenant stipulating a minimum tangible net worth of $6,250,000 with escalations as defined in the Agreement.

The outstanding balance at December 31, 2001, was $7,567,111.

NOTE 5 - EQUITY

Stock options and warrants were exercised during the third quarter of fiscal year 2002. 293,700 shares of common stock were issued with proceeds to the Company of $575,338. The total of Stock options and warrants exercised for the nine month period ended December 31, 2001 were 682,200 shares with a total proceeds to the Company of $956,078.

On August 15, 2001, the directors of the Company were each issued 10,000 common stock options (50,000 options total) at the then current stock price of $6.35. Pursuant to APB no. 25, no compensation expense was recognized.

The 1,656,000 public warrants expired on November 10, 2001.

NOTE 6 - CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The Company has an agreement with FLX (a China manufacturer of consumer electronics products) to produce electronic recording equipment based on the Company's specifications. A former director of the Company, is Chairman of the

Board and a principal stockholder of FLX. During the fiscal year ended March 31, 2001, the Company purchased approximately 80% of its equipment from FLX. The Company anticipates the purchase level to remain close to this number for fiscal year 2002. The amount due to FLX at September 30, 2001 of $673,113 is included in the related party payable. The Company believes that all of the foregoing transactions with FLX have been on terms no less favorable to the Company than could have been obtained from unaffiliated third parties in arms-length transactions under similar circumstances.

NOTE 7 - CONCENTRATIONS

As a percentage of total revenues, the Company's net sales in the aggregate to its five (5) largest customers during the quarters ended December 31, 2001 and 2000 were approximately 98% and 81%, respectively. For the nine months ending December 31, 2001 and 2000, two (2) major retailers accounted for 66% and 36% each of total revenues. Because of the seasonality of the Company's sales, these results may be distorted due to the historically low percentage of overall sales during the Company's first fiscal quarter of each year.

The Company currently obtains its debt financing from one lender. Although management believes there are other sources available, a loss of the current credit facility could, in the short term, adversely affect operations until an alternate lending arrangement is secured.

The Company is dependent upon foreign companies for manufacture of all of its electronic products. The Company's arrangements with manufacturers are subject to the risks of doing business abroad, such as import duties, trade restrictions, work stoppages, foreign currency fluctuations, political instability, and other factors which could have an adverse impact on its business. The Company believes that the loss of any one or more of their suppliers would not have a long-term material adverse effect because other manufacturers with whom the Company does business would be able to increase production to fulfill their requirements. However, the loss of certain suppliers, could, in the short-term, adversely affect business until alternative supply arrangements are secured.

During fiscal 2001 and 2000, suppliers in the People's Republic of China (China) accounted for in excess of 94% and 88%, respectively of our total product purchases, including virtually all of our hardware purchases. The Company expects purchasing for fiscal 2002 to fall within the above range as well.

NOTE 8 - EARNINGS PER SHARE

Basic net income (loss) per common share (Basic EPS) excludes dilution and is computed by dividing net income (loss) available to common stockholder by the weighted-average number of common shares outstanding for the period. Diluted net income per share (Diluted EPS) reflects the potential dilution that could occur if stock options or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. At December 31, 2001 there were 1,015,200 common stock equivalents outstanding which may dilute future earnings per share.

NOTE 9 - INCOME TAXES

At March 31, 2001, the Company had useable net operating loss carryforwards of approximately $4,326,370 for income tax purposes, available to offset future taxable income of the U.S. entity expiring through 2021.

The valuation allowance was $1,059,089 at March 31, 2001. This allowance was reversed at December 31, 2001 as management estimates that it is more likely than not that the deferred tax assets will be realized. The deferred tax asset was adjusted based on estimated use of net operating losses through December 31, 2001 to $526,247.

In accordance with SFAS 109, the income tax benefit of $73,574 arising from the net increase in deferred tax assets has been allocated at December 31, 2001 to reduce the reorganization intangible.

NOTE 11 - SEGMENTS

The Company operates in one business segment. Sales during the three months and nine months ended December 31, 2001, were all generated to customers in the United States.

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

EXPLANATORY NOTE

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FORWARD-LOOKING STATEMENTS

Certain statements contained in this Quarterly Report on Form 10- QSB, including without limitation, statements containing the words believes, anticipates, estimates, expects, and words of similar import, constitute forward-looking statements. You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks faced by us described below and elsewhere in this Quarterly Report, and in other documents we file with the Securities and Exchange Commission.

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.

GENERAL

The Singing Machine Company, Inc. and its wholly owned subsidiary, International (SMC) HK, Ltd.(the Company, we or us) engages in the production and distribution of karaoke audio software and electronic recording equipment. Our electronic karaoke machines and audio software products are marketed under The Singing Machine(R) trademark.

Our products are sold throughout the United States, 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 retail outlets as Best Buy, Toys R Us, Target, J.C. Penney and Fingerhut.

We had a net profit before estimated income tax of $8,287,447 for the nine month period ended December 31, 2001. Our working capital as of December 31, 2001, was approximately $16,649,546.

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RESULTS OF OPERATIONS

REVENUES

Revenues for the three months ended December 31, 2001 (the third quarter) were $34,158,513, an increase of 146% over the third quarter of fiscal 2001. Revenues for the nine months ended December 31, 2001 were $55,431,595, an increase of 80% over the first nine months of fiscal 2001. The Company's growth was driven by the addition of new products to the core product line and a larger concentration of our product with both our existing and new customers. A strong sell through of our product on the store level also added to increased purchasing from our largest customers on down. Other factors contributing to the increased sales include the strong sales of MTV licensed merchandise. We believe that the strong popularity of our products contributed greatly to our sales growth.

GROSS PROFIT

Gross profit for the three month period ended December 31, 2001 was $11,438,583 or 34% of sales compared with $4,689,936 or 34% of sales for the third quarter of the prior year. Gross profit for the nine months ended December 31, 2001 and 2000 were $18,609,980, or 34% of revenues and $9,513,763, or 31% of revenues, respectively. This favorable increase in the Company's gross profit margin is due to increased purchasing efficiencies and to the increased sale of music products which have higher profit margins than some of our electronic products. It is also due to the elimination of manufacturers' agency fees which were a part of product cost in prior years and a different mix of products.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses (SG&A) were $5,422,298 or 15.9% of total revenues, in the third quarter, up from $2,259,606 or 16.3% of total revenues, in the third quarter of the prior year. For the nine months ended December 31, 2001, SG&A were $10,415,804 or 18.8% of total revenues, up from $4,806,054 or 15.6% of total revenues for the nine months ended December 31, 2000. The increase in SG&A expenses is primarily due to costs associated with: (1) with opening the Company's Hong Kong office, (2) the Company's first advertising campaign, (3) the amortization of certain guarantee fees and (4) certain expenses associated with increased sales.

In December 2000, the Company's wholly-owned subsidiary, International SMC (HK) Ltd. opened a Hong Kong office. In the third quarter of fiscal 2002, this office incurred SG&A expenses of approximately $506,000 over the same period of the prior year. By opening this office, the Company saves the manufacturers agency fees which were paid in prior years. The Hong Kong office has fixed overhead expenses every month, as opposed to per shipment agency fees. The benefit can be seen in the third quarter as the Company has the greatest amount of purchases from China.

For the first time in its history, the Company has embarked on a formal advertising campaign, which uses print advertising, radio spots, sponsorships, promotions and other media. The cost of advertising during the third quarter was approximately $363,000.

Other factors contributed to the increased SG&A expenses when comparing the quarter ended December 31, 2001 and 2000. These factors include payroll and its associated expenses which contributed approximately $395,000 in expenses in the third quarter primarily due to the addition of personnel. Other increases in SG&A expenses were variable expenses which are directly related to the increase in sales. The largest of these variable expenses, royalty expense, increased $1,138,000 in the third quarter of 2001 as compared to the third quarter of 2000 primarily from the sale of items under the MTV licensing agreement. This is the first year of sales of MTV branded product. Commission expense is a variable expense, which contributed $777,000 to the third quarter increase in SG&A. Other variable expenses include various warehouse expenses.

DEPRECIATION AND AMORTIZATION EXPENSES

The Company's depreciation and amortization expenses were $236,032 or .7 % of total revenues in the third quarter, up from $54,281 or .4% in the third quarter of the prior year. For the nine months ended December 31, 2001, the Company's depreciation and amortization expenses were $451,154, or .8% of total revenues, up from $132,244, or .4% of total revenues, for the nine months ended December 31, 2000. The increase in depreciation and amortization expenses can be attributed to the Company's acquisition of new fixed assets during the last twelve months, which included computers, furniture and other equipment in all of the Company's locations in Florida, California and Hong Kong. It also included the addition of new molds for our expanded product line. The amortization expense also includes the amortization of a fee paid to LaSalle Bank for our line of credit facility and the amortization of remaining deferred guarantee fees related to the factor agreement we terminated in April 2001.

OTHER INCOME AND EXPENSES

Other expenses were $33,806 for the third quarter of fiscal 2002 compared with net expenses of $328,677 for the third quarter of the prior year. Other income was $93,271 for the nine months ended December 31, 2001 compared with net

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expenses of $561,206 for the nine months ended December 31, 2000. The Company has begun to generate positive income from these miscellaneous items because it has had a decrease in factoring fees and interest expense. The Company no longer has to pay factoring fees because it terminated its factoring agreement in the first quarter of 2002, when it entered into its credit facility with LaSalle National Bank. Furthermore, the Company's interest expense during the first nine months is much lower than the prior year because of favorable rates under its credit facility with LaSalle. The Company has also begun to generate income from royalty payments received in Hong Kong for the use of Company owned molds by other parties.

INCOME BEFORE INCOME TAX EXPENSE

The Company's net income before income taxes increased 184.7% to $5,982,480 for the third quarter compared with $2,101,653 for the third quarter of the previous year. The Company's net income before income taxes increased 99.9% to $8,287,447 for the nine months ended December 31, 2001 compared with $4,146,503 for the nine months ended December 31, 2000. This increase in profit is due primarily to the increase in sales.

INCOME TAX EXPENSE

The Company files separate tax returns for the parent and for the Hong Kong Subsidiary.

During the third quarter of fiscal 2002, the Company showed a loss in the U.S. parent company, and a profit in International SMC (HK) Ltd., its wholly-owned Hong Kong subsidiary. As a result of this, the accrual for income tax included an estimate for alternative minimum tax in the U.S.A. and a provision for income tax for the subsidiary income. No change was made in the deferred tax asset as the change was not material.

In April 2001, International SMC applied for an offshore tax exemption, based on the locality of profits of the Hong Kong subsidiary. Management believed that the exemption would be approved because the source of all profits of the Hong

Kong subsidiary is from exporting to customers outside of Hong Kong. Accordingly, no provision for income taxes was provided in quarterly report for the quarter ended December 31, 2001. Management is continuing its exemption application process. However, due to the extended period of time that the application has been outstanding, as well as management's reassessment of the probability that the application will be approved, management determined to restate the fiscal year 2002 and 2001 consolidated financial statements and certain related quarterly financial statements for fiscal 2002 and 2003 to provide for such taxes. The net effect of the above two adjustments is to decrease net income by $1,286,119 for the quarter ended December 31, 2001 and $1,874,741 for the nine months then ended.

With regard to United States taxation of foreign income, the Company had originally taken the position that the foreign income of the Hong Kong subsidiary qualified for a deferral under the Internal Revenue Code allowing for such income to be indefinitely deferred and not taxed in the United States until such income is repatriated. Full disclosure of the amount and nature of the indefinite deferral for fiscal year 2002 was reflected in the income tax footnote of the consolidated financial statements for that year. The Internal Revenue Code, regulations and case law regarding international income taxation is quite complex and subject to interpretation. Each case is determined based on the individual facts and circumstances. Due to certain inter-company loans made in 2002 and 2003, the profits previously considered to be indefinitely deferred became partially taxable as "deemed dividends" under section 956 of the Internal Revenue Code. Although certain arguments against the imposition of a "deemed dividend" may be asserted, management has determined to restate the fiscal year 2002 consolidated financial statements based on its reassessment of its original position. The effect of such restatement is to increase income tax expense by $1,006,979 for the nine months ended December 31, 2001, which includes the utilization of the foreign tax credits referred to above.

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SEASONALLY AND QUARTERLY RESULTS

Historically, the Company's operations have been seasonal, with the highest net sales occurring in the second and third quarters (reflecting increased orders for equipment and music merchandise during the Christmas selling months) and to a lesser extent the first and fourth quarters of the fiscal year.

The Company's 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.

FINANCIAL CONDITION AND LIQUIDITY

At December 31, 2001, the Company had current assets of $36,169,660 and total assets of $37,835,772 compared to current assets of $9,023,749 and total assets of $10,509,682 at March 31, 2001. This increase in current assets and total assets is primarily due to the increase in accounts receivable for sales in the months of November and December. The average collection period for receivables is 45 days and as of January 31, 2002, over $15,000,000 of the accounts receivable balance has been collected. Another factor in the increase of current assets is the increase in inventory for future shipments.

Current liabilities increased to $19,520,114 as of December 31, 2001, compared to $1,591,021 at March 31, 2001. This increase in current liabilities is because of increased accounts payable and accrued expenses for the third quarter. The use of the credit line was primarily to purchase inventory. Accounts payable increased to $7,049,514 as of December 31, 2001 from $821,684 as of March 31, 2001, primarily as a consequence of the Company's increased expenditures to finance its sales efforts and the purchase of music inventory in the United States. Increased accrued expenses include a royalty expense payable to MTV for the sale of licensed merchandise, as well as other agencies and publishers with whom we hold licenses for our recorded music.

The Company's stockholders' equity increased to $18,315,658 as of December 31, 2001 from $8,918,661 as of March 31, 2001, due to the exercise of warrants, the write off of deferred guarantee fees and the current year to date net income.

Cash flows used in operating activities were $8,105,301 during the nine months ended December 31, 2001. Cash flows were used in operating activities primarily by an increase in accounts receivable in the amount of $26,104,253 and inventory in the amount of $1,900,092. Cash flows were provided by operating activities primarily by an increase in accounts payable and accrued expenses in the amount of $9,712,189 and net income of $8,269,447. These increases are a direct result of the increased volume of sales for the period.

Cash provided by investing activities during this same period was $482,596 resulting primarily from receipt of $933,407 previously invested with the Company's factor. Other factors included in this increase included $117,425 received from our officers as repayments on loans and $274,702 received from the sale of an unconsolidated subsidiary. Cash used for investing activities consisted of property and equipment in the amount of $593,823 and a $256,807 deposit placed for a credit line.

Cash flows provided by financing activities were $8,523,189 during the nine month period ended December 31, 2001. This consisted of proceeds from the exercise of warrants and options in the amount of $956,078 and the net amount of borrowing on the line of credit at LaSalle Bank in the amount of $7,567,111.

CAPITAL RESOURCES

The Company has obtained significant financing for continuing operations and growth. In April 2001, the Company entered into a credit facility with LaSalle Business Credit, Inc., which replaced the Company's pre-existing financing arrangements with Main Factors, Inc. and EPK Financial. The Company also has a credit facility with Belgian Bank, which is not currently in use and the terms of which are being renegotiated.

LASALLE BANK

The Company entered into a credit facility with LaSalle Business Credit, Inc. (the Lender or LaSalle) in April 2001. Under this credit facility, the Lender will advance up to 75% of the Company's eligible accounts receivable, plus up to 40% of eligible inventory, plus up to 40% of commercial letters of credit issued by the Lender minus reserves as set forth in the loan documents.

The credit facility is subject to loan limits from zero to $10,000,000 depending on the time of the year, as stipulated in the loan documents.

Advances made under the credit facility bear interest at the lender's prime rate plus .5%. There is also an annual fee of 1% of the loan maximum, or $100,000.

The credit facility expires on April 26, 2004 and is automatically renewable for one-year terms thereafter. Under the terms of the credit facility, the Company is required to maintain certain financial ratios and conditions. The loan contains a clean up period every 12 months where the loan amount must go to zero for a period of time. The loan is secured by a first lien on all present and future assets of the Company, except certain tooling located in China.

The Company has no present commitment that is likely to result in its liquidity increasing or decreasing in any material way. In addition, the Company knows of no trend, additional demand, event or uncertainty that will result in, or that is reasonably likely to result in, the Company's liquidity increasing or decreasing in any material way.

The Company has no material commitments for capital expenditures. The Company knows of no material trends, favorable or unfavorable, in the Company's capital resources. The Company has no additional outstanding credit lines or credit commitments in place and has no additional current need for financial credit. In next few months, the Company may obtain additional credit facilities for its Hong Kong subsidiary, but this will not have a significant impact on its liquidity.

FORTIS BANK, HONG KONG

Effective February 14, 2000, the Company, through its Hong Kong subsidiary, obtained a credit facility of $500,000 (US) from Fortis Bank, Hong Kong, formerly known as Belgian Bank, Hong Kong, a subsidiary of Generale Bank, Belgium. This facility is a revolving line based upon drawing down a maximum of 15% of the value of export letters of credit held by Belgian Bank. There is no maturity date except that Belgian Bank reserves the right to revise the terms and conditions at the Bank's discretion.

The cost of this credit facility is the U.S. Dollar prime rate plus 1.25%. Repayment of principal plus interest shall be made upon negotiation of the export letters of credit, but not later than ninety (90) days after the advance. This credit facility is not currently in use and the terms are being renegotiated.

RISK FACTORS

Set forth below and elsewhere in this Quarterly Report and in the other documents we file with the SEC are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward looking statements contained in this Quarterly Report.

FACTORS THAT MAY AFFECT FUTURE RESULTS AND MARKET PRICE OF STOCK

Our inability to compete and maintain our niche in the entertainment industry could hurt our business

The business in which we are engaged is highly competitive. 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 and prerecorded tapes, CD's and video cassettes. Competition in the karaoke industry is based primarily on price, product performance, reputation, delivery times, and customer support. We believe that our new product introductions and enhancements of existing products are material factors for our continuing growth and profitability. Many of our competitors are substantially larger and have significantly greater financial, marketing and operating resources than we have. No assurance can be given that we will continue to be successful in introducing new products or further enhancing existing products.

We rely on sales to key customers which subjects us to risk

As a percentage of total revenues, our net sales to our five largest customers during the nine months ended December 31, 2001 and 2000, were approximately 98% and 81% respectively. During fiscal year 2002, we further intend to broaden our base of customers. Although we have long-established relationships with many of our customers, we do not have long-term contractual arrangements with any of them. A decrease in business from any of our major customers could have a material adverse effect on our results of operations and financial condition.

We have significant reliance on large retailers which are subject to changes in the economy

We sell products to retailers, including department stores, lifestyle merchants, direct mail retailers which are catalogs and showrooms, national chains, specialty in stores, and warehouse clubs. Certain of such retailers have engaged in leveraged buyouts or transactions in which they incurred a significant amount of debt, and some are currently operating under the protection of bankruptcy laws. Despite the difficulties experienced by retailers in recent years, we have not suffered significant credit losses to date. Deterioration in the financial condition of our major customers could have a material adverse effect on our future profitability.

We may not be able to sustain or manage our rapid growth

We experienced rapid growth in net sales and net income in the last year. As a result, comparing our period-to-period operating results may not be meaningful, and results of operations from prior periods may not be indicative of future results. We cannot assure you that we will continue to experience growth in, or maintain our present level of, net sales or net income.

Our growth strategy calls for us to continuously develop and diversify our karaoke products by (i) developing new karaoke machines and software products, (ii) entering into additional license agreements and (iii) expanding into international markets, which will place additional demands on our management, operational capacity and financial resources and systems. The increased demand on management may necessitate our recruitment and retention of additional qualified management personnel. We cannot assure you that we will successfully recruit and retain qualified personnel or expand and manage our operations effectively and profitably.

In addition, implementation of our growth strategy is subject to risks beyond our control, including competition, market acceptance of new products, changes in economic conditions, our ability to obtain or renew licenses on commercially reasonable terms and our ability to finance increased levels of accounts receivable and inventory necessary to support our sales growth, if any. Accordingly, we cannot assure you that our growth strategy will be implemented successfully.

The market price of our common stock may be volatile

Market prices of the securities of companies in the toy and entertainment industry are often volatile. The market prices of our common stock may be affected by many factors, including:

- fluctuations in our financial results;

- the actions of our customers and competitors (including new product line announcements and introduction);

- new regulations affecting manufacturing;

- other factors affecting the toy and entertainment industry in general; and

- sales of our common stock into the public market.

In addition, the stock market periodically has experienced significant price and volume fluctuations which may have been unrelated to the operating performance of particular companies.

We are subject to the risks of doing business abroad

We are dependent upon foreign companies for manufacture of all of our electronic products. Our arrangements with manufacturers are subject to the risks of doing business abroad, such as import duties, trade restrictions, work stoppages, foreign currency fluctuations, political instability, and other factors which could have an adverse impact on our business. We believe that the loss of any one or more of our suppliers would not have a long-term material adverse effect on us because other manufacturers with whom we do business would be able to increase production to fulfill our requirements. However, the loss of certain of our suppliers, could, in the short-term, adversely affect our business until alternative supply arrangements were secured.

During fiscal 2001 and 2000, suppliers in the People's Republic of China (China) accounted for in excess of 94% and 88%, respectively of our total product purchases, including virtually all of our hardware purchases. The Company expects purchasing for fiscal 2002 to fall within the above range as well.

At the fourth ministerial conference of the World Trade Organization (WTO) held November 9 through 14, 2001 the accession of China and Chinese Taipei were approved. This addition to the WTO should help facilitate our business operations in China.

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We have significant future capital needs which are subject to the uncertainty of additional financing

We may need to raise significant additional funds to fund our rapid sales growth and/or implement other business strategies. If adequate funds are not available on acceptable terms, or at all, we may be unable to sustain our rapid growth, which would have a material adverse effect on our business, results of operations, and financial condition.

We are subject to seasonality which is affected by various economic conditions and changes resulting in fluctuations in quarterly results

We have experienced, and will experience in the future, significant fluctuations in sales and operating results from quarter to quarter. This is due largely to the fact that a significant portion of our business is derived from a limited number of relatively large customer orders, the timing of which cannot be predicted. Furthermore, as is typical in the karaoke industry, the quarters ended September 30 and December 31 will include increased revenues from sales made during the holiday season. Additional factors that can cause our sales and operating results to vary significantly from period to period include, among others, the mix of products, fluctuating market demand, price competition, new product introductions by competitors, fluctuations in foreign currency exchange rates, disruptions in delivery of components, political instability, general economic conditions, and the other considerations described in this section entitled Risk Factors.

Accordingly, period-to-period comparisons may not necessarily be meaningful and should not be relied on as indicative of future performance. Historically, the first and fourth quarters of our fiscal year have been the least profitable quarter and the second and third have been the most profitable.

Our proprietary technology may not be sufficiently protected

Our success depends on our proprietary technology. We rely on a combination of contractual rights, trade secrets, know-how, trademarks, non-disclosure agreements and technical measures to establish and protect our rights. We cannot assure you that we can protect our rights to prevent third parties from using or copying our technology.

We may be subject to claims from third parties for unauthorized use of their proprietary technology, copyrights or trade secrets

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 assure you that we have not infringed on the proprietary rights of third parties or those third parties will not make infringement violation claims against us. Any infringement claims may have a negative effect on our ability to manufacture our products.

We may be infringing upon the copyrights of third parties

Each song in our catalog is licensed to us for specific uses. Because of the numerous variations in each of our licenses for copyrighted music, there can be no assurance that we have complied with scope of each of our licenses. Additionally, third parties over whom we exercise no control may use our sound recordings in such a way that is contrary to our license agreement and by violating our license agreement we may be liable for contributory copyright infringement. Any infringement claims may have a negative effect on our ability to sell products.

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 audio software and electronic recording equipment 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. Adverse economic changes affecting these factors may restrict consumer spending and thereby adversely affect our growth and profitability.

We depend on third party suppliers to manufacture 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 us 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. If we are unable to purchase the supplies and parts we need to manufacture our karaoke machines and related products, we will experience severe production problems, which may possibly result in the termination of our operations.

Our business operations could be significantly disrupted if we lose members of our management team

Our success depends to a significant degree upon the continued contributions of our executive officers, both individually and as a group. Although we have entered into employment contracts with Edward Steele, our Chief Executive

Officer and John Klecha, our President, Chief Operating Officer, Chief Financial Officer, Treasurer and Secretary, and the loss of the services of either of these individuals could prevent us from executing our business strategy.

Your investment may be diluted

If additional funds are raised through the issuance of equity securities, your percentage ownership in our equity will be reduced. Also, you may experience additional dilution in net book value per share, and these equity securities may have rights, preferences, or privileges senior to those of yours.

RISKS ASSOCIATED WITH OUR CAPITAL STRUCTURE

Future sales of our common stock held by current stockholders may depress our stock price

As of December 31 2001, there were 5,041,320 shares of our common stock outstanding,. We have filed two registration statements to register an aggregate of 3,194,823 shares of our common stock (a registration statement on Form S-3 to register the resale of 1,965,323 shares or our common stock and a registration statement on Form S-8 to register the sale of 1,229,500 shares underlying options granted under our 1994 Stock Option Plan). We also intend to file a registration statement on Form S-8 to register 1,300,000 shares of our common stock underlying options granted under our Year 2001 Stock Option Plan. 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.

ADVERSE EFFECT ON STOCK PRICE FROM FUTURE ISSUANCES OF ADDITIONAL SHARES

Our Certificate of Incorporation authorizes the issuance of 18,900,000 million shares of common stock. As of December 31, 2001, we had 5,041,320 shares of common stock issued and outstanding and an aggregate of 1,015,200 outstanding options and warrants. As such, our Board of Directors has the power, without stockholder approval, to issue up to 12,843,480 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 may 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.

We are also subject to certain provisions of Delaware law that could delay, deter or prevent us from entering into an acquisition, including the Delaware General Corporation Law, which prohibits a Delaware corporation from engaging in a business combination with an interested stockholder unless specific conditions are met. The existence of these provisions could limit the price that investors are willing to pay in the future for shares of our common stock and may deprive you of an opportunity to sell your shares at a premium over prevailing prices.

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PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is not a party to any material legal proceeding, nor to the knowledge of management, are any legal proceedings threatened against the Company. From time to time, the Company may be involved in litigation relating to claims arising out of operations in the normal course of business.

ITEM 2. CHANGES IN SECURITIES

(a) Not Applicable.

(b) Not Applicable.

(c) During the three month period ended December 31, 2001, seven employees exercised stock options issued under our 1994 Amended and Restated Management Stock Option Plan. The employees exercised options to acquire an aggregate of 62,300 shares of our common stock. The names of the option holders, the dates of exercise the number of shares purchased, the exercise price and the proceeds received by the Company are listed below.

Name	Date of Exercise	No. of Shares	Exercise Price	Proceeds
April Green	10/02/01	1,000	$1.66	$ 1,660
April Green	10/31/01	1,000	$1.66	$ 1,660
John Steele	11/06/01	10,000	$1.66	$16,600
Brian Cino	11/13/01	350	$ .43	$ 151
April Green	11/13/01	1,000	$1.66	$ 1,660
Teresa Marco	11/13/01	10,000	$1.66	$16,600
John Steele	12/07/01	5,000	$3.06	$15,300
April Green	12/07/01	700	$1.66	$ 1,162
Melody Rawski	12/18/01	5,000	$3.06	$15,300
April Green	12/18/01	2,000	$3.06	$ 6,120
Edwin Young	12/28/01	25,000	$3.06	$76,500
Adolph Nelson	12/28/01	1,250	$3.06	$ 3,825

Each of these employees paid for the shares with cash. Each of the employees exercised their options in reliance upon Section 4(2) of the Securities Act of 1933, because each of them was knowledgeable, sophisticated and had access to comprehensive information about the Company. The shares issued to our employees were registered under the Securities Act on a registration statement on Form S-8. As such, no restrictive legends were placed on the shares.

On December 28, 2001, Josef Bauer exercised 10,000 stock options acquired under our Year 2001 Stock Option Plan. Mr. Bauer exercised his options in reliance upon Section 4123 of the Securities Act of 1933, because he was knowledgeable, sophisticated and had access to comprehensive information about the Company. The Company placed legends on the certificates stating that the securities were not registered under the Securities Act and set forth their restrictions on transferability and sale.

During the three month period ended December 31, 2001, six warrant holders exercised their warrants to acquire an aggregate of 221,400 shares of our common stock. The names of the warrant holders, the dates of exercise the number of shares purchased, the exercise price and the proceeds received by the Company are listed below.

Name	Date of Exercise	No. of Shares	Exercise Price	Proceeds
Edward Borelli	10/29/01	95,400	$ 1.375	$131,175
Anthony Broy	10/31/01	4,000	$ 2.00	$ 8,000
SISM Research	11/02/01	10,000	$ 2.00	$ 20,000
Clarion Finanz AG	11/08/01	67,000	$ 1.375	$ 92,125
Neil Berkman	11/30/01	25,000	$ 3.06	$ 76,500
FRS Investments	12/31/01	20,000	$ 1.375	$ 27,500

Each of the warrant holders paid for their shares with cash. Each of these warrant holders exercised their warrants in reliance upon Section 4(2) of the Securities Act of 1933, because each of these holders was knowledgeable, sophisticated and had access to comprehensive information about the Company. The Company placed legends on the certificates stating that the securities were not registered under the Securities Act and set forth the restrictions on their transferability and sale. We have registered these shares for resale on a registration statement on Form S-3.

(d) Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

EXHIBIT NO. DESCRIPTION

31.1	Certification of Yi Ping Chan, Chief Executive Officer and Chief Operating Officer of The Singing Machine Company, Inc., Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.*
31.2	Certification of April Green, Chief Financial Officer of The Singing Machine Company, Inc., Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934.*
32.1	Certification of Yi Ping Chan, Chief Executive Officer and Chief Operating Officer of The Singing Machine Company, Inc., Pursuant to 18 U.S.C. Section 1350.*
32.2	Certification of April Green, Chief Financial Officer of The Singing Machine Company, Inc., Pursuant to 18 U.S.C. Section 1350.*

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*Filed herewith

(b) Reports on Form 8-K

The Company did not file any Report on Form 8-K during the three months ended December 31, 2001.

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SIGNATURES

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

THE SINGING MACHINE COMPANY, INC.

Dated: March 19, 2004 By: /s/ April J Green

April J Green
Chief Financial Officer,
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX

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32.1	Certification of Yi Ping Chan, Chief Executive Officer and Chief Operating Officer of The Singing Machine Company, Inc., Pursuant to 18 U.S.C. Section 1350.

32.2	Certification of April Green, Chief Financial Officer of The Singing Machine Company, Inc., Pursuant to 18 U.S.C. Section 1350.