

Edgar Filing: AIRTRAX INC - Form 10QSB

AIRTRAX INC
Form 10QSB
November 20, 2006

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

FORM 10-QSB

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended September 30, 2006.

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

Commission file number: 001-16237

AIRTRAX, INC.
(Name of Small Business Issuer in its charter)

| | |
|--|---|
| New Jersey ----- (State or other jurisdiction of incorporation or organization) | 22-3506376 ----- (IRS Employer Identification No.) |
|--|---|

200 Freeway Drive, Unit One, Blackwood, NJ 08012

(Address of principal executive offices)

(856) 232-3000
(Issuer's telephone
number)

Check whether 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 such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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 No

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: As of November 10, 2006, the issuer had 24,015,019 shares of common stock, no par value, issued and outstanding.

Transitional Small Business Issuer Format (Check One): Yes No

AIRTRAX, INC.
SEPTEMBER 30, 2006 QUARTERLY REPORT ON FORM 10-QSB

Edgar Filing: AIRTRAX INC - Form 10QSB

TABLE OF CONTENTS

| | PAGE |
|---|------|
| PART I - FINANCIAL INFORMATION | |
| Item 1. Financial Statements (Unaudited) | |
| Balance Sheets | 3 |
| Statements of Operations and Deficit Accumulated During Development Stage | 4 |
| Statements of Cash Flows | 6 |
| Notes to Financial Statements | 7 |
| Special Note Regarding Forward Looking Statements | |
| Item 2. Management's Discussion and Analysis or Plan of Operation | 12 |
| Item 3. Controls and Procedures | 22 |
| PART II - OTHER INFORMATION | |
| Item 1. Legal Proceedings | 23 |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | 23 |
| Item 3. Defaults Upon Senior Securities | 23 |
| Item 4. Submission of Matters to a Vote of Security Holders | 23 |
| Item 5. Other Information | 23 |
| Item 6. Exhibits | 24 |
| SIGNATURES | 24 |

2

PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS AIRTRAX, INC.

FINANCIAL STATEMENTS
SEPTEMBER 30, 2006
(Unaudited)
AIRTRAX, INC.
BALANCE SHEET

September 30,
2006
(Unaudited)

ASSETS
Current Assets

Edgar Filing: AIRTRAX INC - Form 10QSB

| | | | |
|---|---|----|--------------|
| Cash | | \$ | -- |
| Accounts receivable | | | 192,998 |
| Inventory | | | 1,434,644 |
| Vendor advances | | | 205,645 |
| Deferred tax asset | | | 1,523,029 |
| ----- | | | |
| | Total current assets | | 3,356,316 |
| Fixed Assets | | | |
| Office furniture and equipment | | | 157,522 |
| Automotive equipment | | | 21,221 |
| Shop equipment | | | 53,668 |
| Casts and tooling | | | 273,017 |
| ----- | | | |
| | | | 505,428 |
| Less, accumulated depreciation | | | 344,011 |
| ----- | | | |
| | Net fixed assets | | 161,417 |
| Other Assets | | | |
| Advances to Filco Gmbh | | | -- |
| Patents - net | | | 157,063 |
| Deferred Charges | | | -- |
| Deposits | | | 65 |
| ----- | | | |
| | Total other assets | | 157,128 |
| ----- | | | |
| | TOTAL ASSETS | \$ | 3,674,861 |
| ===== | | | |
| LIABILITIES AND STOCKHOLDERS' DEFICIT | | | |
| Current Liabilities | | | |
| Accounts payable | | \$ | 1,104,710 |
| Accrued liabilities | | | 402,614 |
| Obligation for outstanding options | | | 1,362,299 |
| Warrants and conversion option liability | | | 793,677 |
| Bank loan | | | 13,900 |
| Current convertible debt | | | 646,797 |
| Shareholder loans payable | | | 95,213 |
| ----- | | | |
| | Total current liabilities | | 4,419,210 |
| Long Term Convertible Debt | | | 1,746,248 |
| ----- | | | |
| | TOTAL LIABILITIES | | 6,165,458 |
| ----- | | | |
| Stockholders' Deficit | | | |
| Common stock - authorized, 100,000,000 shares without par value; issued and outstanding - 23,860,305 and 21,939,360, respectively | | | 24,883,095 |
| Paid in capital - warrants | | | 1,587,500 |
| Preferred stock - authorized, 500,000 shares without par value; 375,000 issued and outstanding | | | 545,491 |
| Deficit during development stage | | | (16,751,086) |
| Deficit from operations | | | (12,755,597) |
| Total stockholders' deficit | | | (2,490,597) |
| ----- | | | |
| | TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT | \$ | 3,674,861 |
| ===== | | | |

Edgar Filing: AIRTRAX INC - Form 10QSB

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

3

AIRTRAX, INC.
STATEMENTS OF OPERATIONS
For the Nine Month Periods Ended September 30,

| | 2006 | 2005 |
|--|----------------|-----------------|
| | ----- | ----- |
| SALES | \$ 1,271,277 | \$ 1,271,277 |
| COST OF GOODS SOLD | 1,193,815 | 1,193,815 |
| | ----- | ----- |
| Gross Profit | 77,462 | 77,462 |
| | | |
| OPERATING AND ADMINISTRATIVE EXPENSES | 3,503,315 | 3,900,000 |
| | ----- | ----- |
| OPERATING LOSS | (3,425,853) | (3,900,000) |
| OTHER INCOME AND EXPENSE | | |
| Conversion Expense | (961,569) | (5,600,000) |
| Impairment of Filco advances | (2,000,000) | (2,000,000) |
| Interest expense | (165,320) | (165,320) |
| Revaluation income (expense) | 2,511,010 | (2,200,000) |
| Interest income | 85 | 85 |
| Other income | - | - |
| | ----- | ----- |
| LOSS BEFORE INCOME TAXES | (4,041,647) | (11,800,000) |
| INCOME TAX BENEFIT (STATE): | | |
| Current | 545,727 | 3,000,000 |
| | ----- | ----- |
| LOSS BEFORE DIVIDEND | (3,495,920) | (11,400,000) |
| DEEMED DIVIDENDS ON PREFERRED STOCK | 652,310 | 4,000,000 |
| NET LOSS | (4,148,230) | (11,900,000) |
| PREFERRED STOCK DIVIDENDS PAID | (143,750) | (143,750) |
| ACCUMULATED DEFICIT | \$ (4,291,980) | \$ (12,000,000) |
| | ===== | ===== |
| | | |
| LOSS PER COMMON SHARE | | |
| NET LOSS | \$ (4,148,230) | \$ (11,900,000) |
| ADJUSTMENTS FOR PREFERRED DIVIDENDS ACCUMULATED BUT UNPAID | (70,313) | (70,313) |
| | ----- | ----- |
| NET LOSS ALLOCABLE TO COMMON SHAREHOLDERS | \$ (4,218,543) | \$ (12,000,000) |
| | ===== | ===== |

Edgar Filing: AIRTRAX INC - Form 10QSB

| | | | |
|---|----|------------|------|
| NET LOSS PER SHARE - Basic and Diluted | \$ | (.19) | \$ |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | | 22,694,207 | 18,1 |

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

4

AIRTRAX, INC.
STATEMENTS OF OPERATIONS
For the Three Months Ended September 30,

| | 2006 | 2005 | |
|--|--------------|----------------|--|
| | ----- | ----- | |
| SALES | \$ -- | \$ -- | |
| COST OF GOODS SOLD | -- | -- | |
| | | | |
| OPERATING AND ADMINISTRATIVE EXPENSES | 1,302,610 | 1,917,313 | |
| | ----- | ----- | |
| OPERATING LOSS | (1,302,610) | (1,917,313) | |
| OTHER INCOME AND EXPENSE | | | |
| Conversion expense | (201,385) | -- | |
| Impairment of Filco advances | (1,000,000) | | |
| Interest expense | (58,045) | (16,235) | |
| Revaluation (expense) income | 1,404,971 | (1,638,750) | |
| Interest income | -- | 1,662 | |
| Other income | -- | -- | |
| | ----- | ----- | |
| LOSS BEFORE INCOME TAXES | (1,157,069) | (3,570,636) | |
| INCOME TAX BENEFIT (STATE): | | | |
| Current | 196,477 | 147,392 | |
| | ----- | ----- | |
| LOSS BEFORE DIVIDEND | (960,592) | (3,423,244) | |
| DEEMED DIVIDENDS ON PREFERRED STOCK | -- | -- | |
| | ----- | ----- | |
| NET LOSS | (960,592) | (3,423,244) | |
| PREFERRED STOCK DIVIDENDS PAID | -- | -- | |
| | ----- | ----- | |
| ACCUMULATED DEFICIT | \$ (960,592) | \$ (3,423,244) | |
| | ===== | ===== | |
| | | | |
| LOSS PER COMMON SHARE | | | |
| NET LOSS | \$ (960,592) | \$ (3,423,244) | |
| ADJUSTMENTS FOR PREFERRED DIVIDENDS ACCUMULATED BUT UNPAID | (23,438) | (23,438) | |
| | ----- | ----- | |

Edgar Filing: AIRTRAX INC - Form 10QSB

| | | |
|---|--------------|----------------|
| LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS | \$ (984,030) | \$ (3,446,682) |
| | ===== | ===== |
| NET LOSS PER SHARE - Basic and Diluted | \$ (.04) | \$ (.16) |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | 23,573,718 | 21,740,196 |

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

5

AIRTRAX, INC.
STATEMENTS OF CASHFLOWS
For the Nine Month Periods Ended September 30,

| | 2006 |
|---|----------------|
| | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES | |
| Net (Loss) | \$ (4,148,230) |
| Adjustments to reconcile net income to net cash consumed by operating activities: Charges not requiring the outlay of cash: | |
| Depreciation and amortization | 46,125 |
| Amortization of bond discount | |
| Equity securities issued for services | 1,325,264 |
| Stock issued in settlement of obligations | 66,110 |
| Expense of settling certain liquidated damages | 44,267 |
| Conversion expense | 961,569 |
| Deemed dividend | 652,310 |
| Increase in accrual of deferred tax benefit | (545,727) |
| Impairment | 2,000,000 |
| Revaluation of liabilities for warrants and conversion privileges | (2,511,010) |
| Interest accrued on shareholder loan | 9,193 |
| Changes in current assets and liabilities: | |
| Increase in accounts receivable | (98,641) |
| Increase in vendor advances | (42,128) |
| Increase (decrease) in accounts payable | 219,247 |
| Increase (decrease) in accrued liabilities | 136,058 |
| Decrease (increase) in inventory | 570,495 |
| | ----- |
| Net cash consumed by operating activities | (1,315,098) |
| | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES | |
| Acquisitions of equipment | (12,649) |
| Additions to patent cost | (6,800) |
| Advances to FilCO GmbH | - |
| | ----- |
| Net cash consumed by investing activities | (19,449) |
| | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES | |
| Proceeds of issuance of convertible debt | 1,219,800 |
| Net proceeds of common stock sales | 65,500 |
| Proceeds from exercise of warrants | -- |
| Proceeds of bank loan | 13,900 |
| Proceeds from warrant extensions | 117,000 |
| Proceeds from exercise of options | -- |

Edgar Filing: AIRTRAX INC - Form 10QSB

| | |
|---|-----------|
| Proceeds of stockholder loans | 69,813 |
| Repayment of stockholder loans | (170,754) |
| | |
| Net cash provided by financing activities | 1,315,259 |
| | ===== |
| Net decrease in cash | (19,288) |
| Balance at beginning of period | 19,288 |
| | ----- |
| Balance at end of period | \$ -- |
| | ===== |

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

6

AIRTRAX, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2006
(Unaudited)

1. BASIS OF PRESENTATION

The unaudited interim financial statements of Airtrax, Inc. ("the Company") as of September 30, 2006 and for the three and nine month periods ended September 30, 2006 and 2005 have been prepared in accordance with accounting principles generally accepted in the United States of America. In the opinion of management, such information contains all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results of such periods. The results of operations for the nine month period ended September 30, 2006 are not necessarily indicative of the results to be expected for the full fiscal year ending December 31, 2006.

Certain information and disclosures normally included in the notes to financial statements have been condensed or omitted as permitted by the rules and regulations of the Securities and Exchange Commission, although the Company believes the disclosure is adequate to make the information presented not misleading. The accompanying unaudited financial statements should be read in conjunction with the financial statements of the Company for the year ended December 31, 2005.

2. ACCOUNTING PRONOUNCEMENTS

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123 (R), "Accounting for Stock-Based Compensation," using the modified prospective transition ("MPT") method. This change had a negligible effect on results of operations.

3. CONVERTIBLE NOTE FINANCINGS AND STOCK SALES

During the first six months of 2006, the Company issued \$819,800 of 8% Convertible Notes, due on February 13, 2007. The notes together with related interest thereon have been converted to stock at the specified conversion price of \$1.56. Accompanying the notes were 525,513 warrants to purchase common stock, exercisable at \$1.75 per share for a period of five years, starting immediately.

Previous Convertible Issues had contained "Most Favored Nations" clauses that guaranteed the investors that subsequent issues of stock or notes

Edgar Filing: AIRTRAX INC - Form 10QSB

would not be made on more favorable terms. If the Company subsequently issues any shares of common stock or securities convertible or exercisable into common stock at a per share purchase price which is less than the conversion or exercise prices of outstanding notes and warrants, such conversion or exercise prices would be adjusted downward in accordance with their respective terms. As a result of the issuance of the convertible notes set forth above, the following warrant and conversion prices were adjusted:

1. The exercise price for warrants associated with a May 2005 \$500,000 convertible debenture offering was adjusted from \$2.11 per share to \$1.56 per share.

2. The conversion price for an October 2005 \$1,548,000 issuance of convertible debentures was adjusted from \$2.00 per share to \$1.56 per share.

3. The exercise price for 774,000 warrants issued pursuant to the October 2005 convertible debenture offering was adjusted from \$3.25 per share to \$1.56 per share.

The affect of these changes is included in the calculation of revaluation income.

7

AIRTRAX, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2006
(Unaudited)

3. CONVERTIBLE NOTE FINANCINGS AND STOCK SALES (CONT'D)

Included in funds raised during 2004 through stock sales was \$1,312,000 raised under a Purchase Agreement dated November 22, 2004. That agreement required, among other things, that a registration statement be filed with the SEC and that the registration statement be declared effective by the SEC within a prescribed time. The Company did not satisfy its obligation to cause the SEC to declare the registration statement effective within the timeframe specified in the November 2004 Registration Rights Agreement. As a result, it was subject to, and accruing liquidated damages in an amount equal to 2% of the amount invested for each 30 day period following the default date. On May 31, 2005, the Company entered into a letter agreement with a representative of this shareholder group under which \$120,429 was paid to settle the liquidated damages, which had accrued. Under that agreement, no further liquidated damages would accrue until after June 30, 2005. The obligation concerning effectiveness of the registration statement has not been satisfied and liquidated damages accrued since June 30, 2005 at the rate of approximately \$26,240 per month. The liquidated damages paid thus far, and liquidated damages that accrued subsequent to June 30, 2005, were charged to expense during the periods in which they accrued. For the year ended December 31, 2005 an additional \$160,851 had accrued; and \$88,126 accrued during 2006. All liquidated damages for this issue were settled by the issuance on June 30, 2006 of convertible notes, which are described below.

On March 1, 2006, the Company issued \$150,000 of 4% Convertible Notes due March 1, 2008, accompanied by 48,077 warrants to purchase common stock at \$1.65 over a five year period. On June 30, 2006, the Company issued an additional \$48,248 in 4% convertible notes due September 30, 2008, accompanied by 24,124 warrants exercisable at \$1.65 per share over five

Edgar Filing: AIRTRAX INC - Form 10QSB

years in settlement of the liquidated damages described above. These notes are also convertible at \$1.56 over two years. As of June 30, 2006, all damages payable to all of the investors in the Company's November 2004 private placement have been settled, and pursuant to a modification agreement which the Company entered into with such investors on March 1, 2006 and June 30, 2006, no liquidated damages will accrue for the non-effectiveness of the registration statement after the date of the modification agreements.

The Company's private placements of convertible notes and common stock purchase warrants in 2005 also contained liquidated damages provisions. For two of the financings, February and May, no liquidated damages have accrued despite the fact that the shares underlying the notes and warrants issued in such private placements have not been registered, since the payment of damages is linked to the effectiveness of the registration statement which was initially filed in February 2005 and said registration statement has been withdrawn. Under the third such offering, liquidated damages were effective 150 days after October 18, 2005. Such liquidated damages accrue at the rate of 2% per month of the amount raised in that offering, which was \$1,548,000. Liquidated damages of \$201,240 for the October, 2005 issue have been accrued and charged to expense during the first nine months of 2006.

8

AIRTRAX, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2006
(Unaudited)

3. CONVERTIBLE NOTE FINANCINGS AND STOCK SALES (CONT'D)

During 2006, there have been four issuances of convertible debt. None contains a liquidated damages provision. The first, \$819,800 of 8% convertible debt, has been converted into equity, along with associated interest, at \$1.56 per share, resulting in the issuance of 534,352 additional shares of stock. This issue was accompanied by an equal number of warrants, exercisable at \$1.75 for a period of five years.

A second 2006 issue was \$400,000 of 12% convertible debt due October 20, 2006. After commissions, the Company received net proceeds of \$342,500. The debt is convertible to stock at \$1.56 per share. The issue was accompanied by 282,052 warrants exercisable at \$1.56 for five years.

The third and fourth issues, of 4% convertible debt, which totaled \$198,248, were made in settlement of liquidated damages associated with a November, 2004 issue, as described above.

4. WARRANTS

The Company has issued warrants both as part of "stock units" and as an integral part of convertible note issues. The value of the warrants and conversion options which are classified as liabilities are revalued each reporting period. These values are determined by a Black Scholes valuation model, consistent with the requirements of SFAS No.133.

The following is a summary of warrants outstanding at September 30, 2006:

| | |
|---|-----------|
| Warrants outstanding at December 31, 2005 | 9,503,558 |
| Warrants issued with 2006 convertible notes | 879,765 |

Edgar Filing: AIRTRAX INC - Form 10QSB

Warrants outstanding September 30, 2006

10,383,323
=====

5. SUPPLEMENTAL CASH FLOWS INFORMATION:

There was no interest or taxes paid during the quarters ended September 30, 2006 and September 30, 2005.

There were no noncash investing activities during either the 2006 or 2005 periods. The following noncash financing activities occurred during these periods.

Shares of common stock were issued for services during both the 2006 and 2005 periods. These totaled 670,963 shares and 290,909 shares, respectively.

The Company issued \$198,248 of 4% unsecured debentures, along with 72,201 warrants in settlement of liquidated damages associated with a November, 2004 stock offering. It recorded a charge of \$44,266, representing the difference between accrued damages settled and the combined value of the \$198,248 of debentures issued and the associated derivatives.

9

AIRTRAX, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2006
(Unaudited)

5. SUPPLEMENTAL CASH FLOWS INFORMATION CONTINUED:

The Company converted \$819,800 of convertible debt, along with accrued interest into stock, resulting in the issuance of 534,352 shares of common stock.

An investor converted \$253,303 of convertible debt, along with associated interest to stock, resulting in the issuance of 235,575 shares.

6. OPERATING AND ADMINISTRATIVE EXPENSES

Details of operating and administrative expenses are presented below:

| | Nine Months Ended September 30, 2006 | Nine Months Ended September 30, 2005 |
|----------------------------|---|---|
| Options expense | \$ 48,000 | \$ 1,163,838 |
| Salaries and payroll taxes | 516,882 | 472,634 |
| Impairment | - | 149,589 |
| Marketing expense | 41,873 | 243,761 |
| Development costs | 515,128 | 225,436 |
| Professional fees | 444,786 | 439,980 |
| Commissions | 104,609 | 6,588 |
| Consulting administrative | 257,344 | 348,113 |
| Settlement expense | 44,266 | - |

Edgar Filing: AIRTRAX INC - Form 10QSB

| | | |
|------------------------------------|--------------|-------------|
| Liquidated damages | 282,433 | 199,149 |
| Consulting marketing | - | 306,483 |
| | | 94,080 |
| Rent | 122,320 | 49,377 |
| Insurance | 128,138 | 173,633 |
| Stock-based compensation-directors | 222,500 | - |
| Freight | 55,600 | 107,275 |
| Stock-based compensation-employees | 90,500 | |
| | | |
| Office expense | 53,322 | 91,763 |
| Other expenses | 269,131 | 159,979 |
| | ----- | ----- |
| Totals | \$ 3,503,315 | \$3,925,195 |
| | ===== | ===== |

10

AIRTRAX, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2006
(Unaudited)

7. FILCO INVESTMENT

On February 19, 2004, the Company reached a tentative agreement to purchase capital stock of FilCO GmgH., a German manufacturer of fork trucks (formerly Clark Material Handling Company of Europe) with a manufacturing facility in Mulheim, Germany (FilCO). It was expected that the Company would acquire 75.1% of FilCO. While negotiations were continuing, the Company agreed to make advances to FilCO. Through December 31, 2005 advances totaling \$6,275,881 had thus been made.

On January 20, 2006, Filco filed for insolvency in Germany and a receiver was appointed. As a result, on February 7, 2006 the Company terminated the tentative agreement to acquired Filco stock and began negotiations with the receiver to acquire some or all of the Filco assets. The \$6,275,881 of advances to Filco that were outstanding at December 31, 2005, were secured by liens filed against the machinery and equipment owned by Filco which in 2003 was appraised at \$5,400,000, and by liens filed against its intellectual property, which had not been appraised. Due to the uncertainty of the Company's position under German bankruptcy law, \$4,275,881 of the Filco advances were written off in 2005, and the remaining \$2,000,000 was written off in 2006. In addition, \$413,174 of Company inventory stored at the Filco plant was abandoned and written off during 2006. During 2006, an auction of Filco assets was conducted by the receiver who did not acknowledge the Airtrax liens against property and equipment.

8. SUBSEQUENT EVENTS

The Company is currently in default on its 12% Series A Convertible Note in the principal amount of \$400,000 which the Company issued to a qualified institutional buyer on July 26, 2006. All principal and accrued and unpaid interest was due on October 20, 2006. The Company did not repay the note in the amount of \$412,000, inclusive of principal and accrued and unpaid interest, on or prior to October 20, 2006. The Company is currently in negotiations with the holder to repay the note through the payment of cash, or issuance of shares of common stock, or a combination of both. As of this

Edgar Filing: AIRTRAX INC - Form 10QSB

report, the Company is negotiating the following proposed settlement:

- o Payment of outstanding interest, approx. \$14,000;
- o Partial payment of principal;
- o 75,000 shares of stock per default provisions;
- o Default interest rate prospectively 18%; and
- o Monthly interest payments and an extension fee.

11

Item 2. Management's Discussion and Analysis and Results of Operations

Forward Looking Statements

Special Note on Forward-Looking Statements. Certain statements in "Management's Discussion and Analysis or Plan of Operation" below, and elsewhere in this annual report, are not related to historical results, and are forward-looking statements. Forward-looking statements present our expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historical or current facts. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. Forward-looking statements frequently are accompanied by such words such as "may," "will," "should," "could," "expects," "plans," "intends," "anticipates," "believes," "estimates," "predicts," "potential" or "continue," or the negative of such terms or other words and terms of similar meaning. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, achievements, or timeliness of such results. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of such forward-looking statements. We are under no duty to update any of the forward-looking statements after the date of this annual report. Subsequent written and oral forward looking statements attributable to us or to persons acting in our behalf are expressly qualified in their entirety by the cautionary statements and risk factors set forth below and elsewhere in this annual report, and in other reports filed by us with the SEC.

Overview

Since 1995, substantially all of our resources and operations have been directed towards the development of the Omni-Directional wheel and related components for lift truck and other material handling applications. Many of the components, including the unique shaped wheels, motors, and frames, have been specially designed by us and specially manufactured for us.

Omni-Directional means that vehicles designed and built by us can travel in any direction. Our Omni-Directional vehicles are controlled with a joystick. The vehicle will travel in the direction the joystick is pushed. If the operator pushes the joystick sideways, the vehicle will travel sideways. If the operator were to twist the joystick the vehicle will travel in circles. Our Omni-Directional vehicles have one motor and one motor controller for each wheel. The Omni-Directional movement is caused by coordinating the speed and direction of each motor with joystick inputs which are routed to a micro-processor, then from the micro-processor to the motor controllers and finally to the motor itself.

During 2006, due primarily to severe liquidity constraints, compounded by the illness and subsequent death of our Founder, President and Chairman Peter Amico

Edgar Filing: AIRTRAX INC - Form 10QSB

in this quarter, no commercial Omni-Directional lift trucks were sold in the quarter ended September 30, 2006. We have nine completed units and have nine that are near completion and which could be completed and shipped depending the availability of funding needed to complete production. As of September 30, 2006, we did not have all of the parts required from every vendor for completion of all of the units. The assembly and sale is dependent upon delivery of all of the required parts.

During the third quarter, we continued development of the Cobra and King Cobra scissor lifts and the Omni-Directional power chair. We anticipate incurring more costs on these products and will begin production of the Cobra and King Cobra in 2007. The growth and development of our business will require a significant amount of additional working capital. We currently have limited financial resources and based on our current operating plan, we will need to raise additional capital in order to continue operations. However, we are in discussions with lenders to raise capital in order to continue operating. We currently do not have adequate cash to meet our short or long term objectives. In the event additional capital is raised, it may have a dilutive effect on our existing stockholders. However, there can be no assurance that additional financing will be available at terms that are suitable to the Company.

The assembly of our products is conducted at our leased facilities at 200 Freeway Drive, Blackwood, NJ 08012. To date, approximately 50% of the frames have been manufactured in the USA. These frames are shipped to the Blackwood plant for complete assembly. Previously, partially assembled vehicles were shipped to the Blackwood facility from the Filco plant in Germany. Fourteen were shipped to the USA for final assembly. A total of approximately sixty frames

12

were shipped from Bulgaria to the Filco plant for partial assembly. None of the frames shipped from Bulgaria were within specification. The twenty seven frames shipped to the United States required re-machining in order to make them useable. The balance were rejected and abandoned with other parts inventory totaling approximately \$450,000. The frames and other inventory remained at the Filco facility and were seized by the receiver. Accordingly, any inventory, equipment or outstanding advances to Filco have been written of during this quarter and there is no indication that the proceeds of any inventory or equipment at the Filco plant will be returned to us

We have incurred losses and experienced negative operating cash flow since our formation. For the nine months ended September 30, 2006 and 2005, we had net loss attributable to common shareholders of approximately \$4.2 million and \$12 million, respectively. The net loss in both periods includes revaluation income and losses of approximately \$2.5 million and \$(2.3 million) in 2006 and 2005, respectively, in connection with the repricing of conversion ratios of convertible debenture issues and of warrant conversion prices. The company wrote down the advance to Filco (See note 7 in the financial statements). We expect to continue to incur significant expenses. Our operating expenses have been and are expected to continue to outpace revenue and result in significant losses in the near term. We may never be able to reduce these losses, which will require us to seek additional debt or equity financing. While we are in discussions with several prospective lenders, we do not currently have commitments for these funds and there can be no assurance that additional financing will be available, or if available, will be on acceptable terms. If we are unable to obtain sufficient funds during the next 6 months we will further reduce the size of our organization and may be forced to reduce and/or curtail our production and operations, all of which could have a material adverse impact on our business prospects.

Our principal executive offices are located at 200 Freeway Drive, Unit One,

Edgar Filing: AIRTRAX INC - Form 10QSB

Blackwood, NJ 08012 and our telephone number is (856) 232-3000. We are incorporated in the State of New Jersey.

Company History

We were incorporated in the State of New Jersey on April 17, 1997. On May 19, 1997, we entered into a merger agreement with a predecessor company that was incorporated on May 10, 1995. We were the surviving company in the merger.

Effective November 5, 1999, we merged with MAS Acquisition IX Corp ("MAS"), and were the surviving company in the merger. Pursuant to the Agreement and Plan of Merger, as amended, each share of common stock of MAS was converted to 0.00674 shares of our company. After giving effect to fractional and other reductions, MAS shareholders received 57,280 of our shares as a result of the merger.

In March 2004, we reached an agreement in principal, subject to certain closing conditions, with Fil Filipov to acquire 51% of the capital stock of Filco GmbH, a German corporation. In April 2003, Filco GmbH acquired substantially all of the assets of Clark Material Handling of Europe GmbH which were located at Clark's facility in Rheinstrasse Mulheim a.d. Ruhr, Germany. These assets consisted of all of the tooling, machinery, equipment, inventory, intellectual property, office furniture and fixtures, and personnel necessary to build the entire Clark line of lift trucks, but excluded the building and land, as well as the rights to the Clark name.

In October 2004, Mr. Filipov and we agreed to modify our agreement in principal so as to increase the number of shares of the capital stock of Filco GmbH which we will acquire, if we finalize the acquisition, from 51% to 75.1%. The purpose of this change is to give us control of Filco GmbH in accordance with USGAAP and German law considerations regarding consolidation and capitalization. Further, this change was offered and accepted in consideration of our agreeing to advance Filco additional funds, in the form of a loan, to fund the start up of the Filco operation prior to the consummation of the transaction. All other conditions and terms of the agreement between the parties remained the same.

We loaned Filco GmbH an aggregate principal amount of \$6,275,881 through December 31, 2005, with no loans made by us in 2006, exclusive of interest at 8% per annum, pursuant to a series of secured promissory notes. Security for these loans consisted of Filco's plant machinery, equipment and other plant property, and intellectual property, including designs and drawings. We used proceeds from the private placement offerings that we completed during 2004 and 2005 to fund the Filco loans.

13

On January 20, 2006, Filco filed for insolvency in Germany. As a result of the filing by Filco, we terminated the Acquisition Agreement on February 7, 2006. An auction sale of Filco assets occurred on May 10, 2006. Due to the uncertainty of the Company's position under German bankruptcy law, \$4,275,881 of the Filco advances were written off in 2005, and the remaining \$2,000,000 was written off in 2006. Accordingly, any inventory, equipment or outstanding advances to Filco have been written off during 2006 and there is no indication that the proceeds of any inventory or equipment at the Filco plant will be returned to us.

CRITICAL ACCOUNTING POLICIES

The Securities and Exchange Commission defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

Edgar Filing: AIRTRAX INC - Form 10QSB

Not all of the accounting policies require management to make difficult, subjective or complex judgments or estimates. However, the following policies could be deemed to be critical within the SEC definition.

REVENUE RECOGNITION

Revenue on product sales is recognized when persuasive evidence of an arrangement exists, such as when a purchase order or contract is received from the customer, the price is fixed, title to the goods has changed and there is a reasonable assurance of collection of the sales proceeds. We obtain written purchase authorizations from our customers for a specified amount of product at a specified price and consider delivery to have occurred at the time of shipment. Revenue is recognized at shipment and we record a reserve for estimated sales returns, which is reflected as a reduction of revenue at the time of revenue recognition.

Revenue from research and development activities relating to firm fixed-price contracts are generally recognized as billing occurs. Revenue from research and development activities relating to cost-plus-fee contracts include costs incurred plus a portion of estimated fees or profits based on the relationship of costs incurred to total estimated costs. Contract costs include all direct material and labor costs and an allocation of allowable indirect costs as defined by each contract, as periodically adjusted to reflect revised agreed upon rates. These rates are subject to audit by the other party. Amounts can be billed on a bi-monthly basis. Billing is based on subjective cost investment factors.

RESULTS OF OPERATIONS - THREE MONTHS ENDED SEPTEMBER 30, 2006 COMPARED WITH THREE MONTHS ENDED SEPTEMBER 30, 2005

We had been a development stage company for much of 2005 and all of 2004 periods and had not engaged in full-scale operations for the periods indicated. The revenue for the periods in 2005 and the first three quarters of 2006 have been derived from the sales of Omni-Directional lift trucks. During 2007, we anticipate achieving full production. Consequently, management believes that the year-to-year comparisons described below are not indicative of future year-to-year comparative results.

Revenue

There was no revenue for the three-month period ended September 30, 2006 and for the comparable period in 2005.

Cost of Goods Sold

The Company's cost of goods sold was zero for the three months ended September 30, 2006 and for the three months ended September 30, 2005.

The Company is entitled to a benefit for the effect on income taxes on the net operating loss. Accordingly, a benefit in the amount of \$196,477 has been recorded for the three months ended September 30, 2006 and \$147,392 was recorded during the three months ended September 30, 2005.

Operating and Administrative Expenses.

Operating and administrative expenses which include administrative salaries, depreciation and other expenses for three-month period ended September 30, 2006 totaled approximately \$1.3 million which represents an decrease of approximately

Edgar Filing: AIRTRAX INC - Form 10QSB

\$600,000 from approximately \$1.9 million incurred in the three-month period ended September 30, 2005. The decrease is due primarily to the recording of stock option expenses in 2005, which were not present in the current quarter, partially offset by expenses related and additional expenses in connection with the development of our Cobra and King Cobra scissor lift and Omni-Directional Power Chair development costs.

Loss Before Income Taxes.

Loss before taxes in the three months ended September 30, 2006 was approximately \$(1.2 million) which reflects a decrease of approximately \$2.4 million from approximately \$(3.6 million) in loss before taxes for the three months ended September 30, 2005. The decrease is due primarily to the recording of stock option expenses in 2005, which were not present in the current quarter, and revaluation income and losses recorded in the quarter of approximately \$1.4 million in 2006 compared with a loss of \$(1.6 million) in the same period in 2005, in connection with the repricing of conversion ratios of convertible debenture issues and of warrant conversion prices, partially offset by expenses related to the write down of the Filco advance of \$1,000,000 and additional expenses relating to the development of our Cobra and King Cobra scissor lift and Omni-Directional Power Chair development costs.

Loss Allocable to Common Shareholders

Loss allocable to common shareholders for the three months ended September 30, 2006 was approximately \$(1.0 million), which represents a decrease of approximately \$2.4 million from approximately \$(3.4 million) in loss allocable to shareholders during the three months ended September 30, 2005. The decrease is due primarily to the recording of stock option expenses in 2005, which were not present in the current quarter, and revaluation income and losses recorded in the quarter of approximately \$1.4 million in 2006 compared with a loss of \$(1.6 million) in the same period in 2005, in connection with the repricing of conversion ratios of convertible debenture issues and of warrant conversion prices, partially offset by expenses related to the write down of the Filco advance of \$1,000,000 and additional expenses relating to the development of our Cobra and King Cobra scissor lift and Omni-Directional Power Chair.

RESULTS OF OPERATIONS - NINE MONTHS ENDED SEPTEMBER 30, 2006 COMPARED WITH NINE MONTHS ENDED SEPTEMBER 30, 2005

We had been a development stage company for much of 2005 and all of 2004 periods and had not engaged in full-scale operations for the periods indicated. The revenue for the periods in 2005 and the first quarter of 2006 have been derived from the sales of Omni-Directional lift trucks. During 2007, we anticipate achieving full production. Consequently, management believes that the year-to-year comparisons described below are not indicative of future year-to-year comparative results.

Revenue

Revenue for the nine-month period ended September 30, 2006 were approximately \$1.3 million, representing an increase of approximately \$1.1 million from revenue of \$168,000 for the comparable period in 2005. This increase in revenue, is primarily, attributed to sales of our SIDEWINDER ATX-3000.

Cost of Goods Sold

The Company's cost of goods sold for the nine months ended September 30, 2006 amounted to approximately \$1.2 million, an increase of approximately \$1.1 million from \$160,000 for the nine months ended September 30, 2005. This increase in revenue, is primarily, attributed to sales of our SIDEWINDER ATX-3000.

Edgar Filing: AIRTRAX INC - Form 10QSB

15

The Company is entitled to a benefit for the effect on income taxes on the net operating loss. Accordingly, a benefit in the amount of \$546,000 has been recorded for the nine-month period ended September 30, 2006 and \$372,000 was recorded during the nine-month period ended September 30, 2005.

Operating and Administrative Expenses.

Operating and administrative expenses which include administrative salaries, depreciation and other expenses for nine-month period ended September 30, 2006 totaled \$3.5 million which represents an decrease of Approximately \$400,000 from \$3.9 million incurred in the nine-month period ended September 30, 2005. The decrease is primarily due recording of stock option expenses in 2005, which were not present in the this period, offset partially by additional expenses relating to the increase in production of our SIDEWINDER ATX-3000 and Cobra and King Cobra scissor lift and Omni-Directional Power Chair development costs.

Loss Before Income Taxes.

Loss before taxes in the nine months ended September 30, 2006 was approximately \$(4.2 million) which reflects a decrease of approximately \$7.8 million from approximately \$(12.0 million) in loss before taxes for the nine months ended September 30, 2005. The decrease is due primarily to the recording of stock option expenses in 2005, which were not present in the current period, and revaluation income and losses recorded in the period of approximately \$2.5 million in 2006 compared with a loss of \$(2.3 million) in the same period in 2005, in connection with the repricing of conversion ratios of convertible debenture issues and of warrant conversion prices, partially offset by expenses related to the write down of the Filco advance of \$2,000,000 and additional expenses relating to the development of our Cobra and King Cobra scissor lift and Omni-Directional Power Chair.

Loss Allocable to Common Shareholders.

Loss before taxes in the nine months ended September 30, 2006 was approximately \$(4.2 million) which reflects a decrease of approximately \$7.8 million from approximately \$(12.0 million) in net loss before taxes for the nine months ended September 30, 2005. The decrease is due primarily to the recording of stock option expenses in 2005, which were not present in the current period, and revaluation income and losses recorded in the period of approximately \$2.5 million in 2006 compared with a loss of \$(2.3 million) in the same period in 2005, in connection with the repricing of conversion ratios of convertible debenture issues and of warrant conversion prices, partially offset by expenses related to the write down of the Filco advance of \$2,000,000 and additional expenses relating to the development of our Cobra and King Cobra scissor lift and Omni-Directional Power Chair.

LIQUIDITY AND CAPITAL RESOURCES

Since our inception, we have financed our operations through the private placement of our common stock and sales of convertible debt. During the nine months ended September 30, 2006 and 2005, we raised net of offering costs approximately \$1.3 million and \$4.7 million, respectively, from the private placement of our securities.

During 2000, we were approved by the State of New Jersey for our technology tax transfer program pursuant to which we could sell our net operating losses and research and development credits as calculated under state law. During the third quarter of 2006 and 2005, we recorded credits of \$196,477 and \$147,393,

Edgar Filing: AIRTRAX INC - Form 10QSB

respectively, from the sale of our losses and credits.

We have consistently demonstrated our ability to meet our cash requirements through private placements of our common stock and convertible notes. We have continued to similarly satisfy those requirements during the quarter ended September 30, 2006. However, there can be no assurances that the Company will be successful in raising the required capital to continue our current operating plan.

We anticipate that our cash requirements for the foreseeable future will be significant. In particular, management expects substantial expenditures for inventory, product production, and advertising with production of its Omni-Directional lift truck and the start of Cobra and King Cobra (Scissors-Lift) production.

We will require additional funds to continue our operations beyond the initial production run. We anticipate that operating capital in the amount of approximately \$5 million will be required during the next three months and into calendar year 2007 to sufficiently fund operations. Of the total amount, approximately 10% is projected for parts and component inventory costs, with the balance projected as new product development costs and general operating

16

expenditures, which includes overhead and salaries. We expect to recognize lower per unit manufacturing and part costs in the future due to volume discounts, as well as lower per unit shipping costs as we transition from the initial rate to larger-scale production. While we are in discussions with several prospective lenders, we do not currently have commitments for additional funds and there can be no assurance that additional financing will be available, or if available, will be on acceptable terms. If we are unable to obtain sufficient funds during the next 6 months we will further reduce the size of our organization and may be forced to reduce and/or curtail our production and operations, all of which could have a material adverse impact on our business prospects.

As a result of our liquidity issues, we have experienced delays in the repayment of certain promissory notes upon maturity and payments to vendors and others. If in the future, the holders of our promissory notes may demand repayment of principal and accrued interest instead of electing to extend the due date and if we are unable to repay our debt when due because of our liquidity issues, we may be forced to refinance these notes on terms less favorable to us than the existing notes, seek protection under the federal bankruptcy laws or be forced into an involuntary bankruptcy filing.

The Company is currently in default on its 12% Series A Convertible Note in the principal amount of \$400,000 which the Company issued to a qualified institutional buyer on July 26, 2006. All principal and accrued and unpaid interest was due on October 20, 2006. The Company did not repay the note in the amount of \$412,000, inclusive of principal and accrued and unpaid interest, on or prior to October 20, 2006. The Company is currently in negotiations with the holder to repay the note through the payment of cash, or issuance of shares of common stock, or a combination of both. As of the date hereof, the Company is negotiating the following proposed settlement:

- o Payment of outstanding interest, approx. \$14,000;
- o Partial payment of principal;
- o 75,000 shares of stock per default provisions;
- o Default interest rate prospectively 18%; and
- o Monthly interest payments and an extension fee

The Company will need to raise substantial additional capital to continue the

Edgar Filing: AIRTRAX INC - Form 10QSB

commence substantial production and development of its products beyond the third quarter of 2006 and provide substantial working capital for the development of national advertising and marketing programs, increases in operating costs resulting from additional staff until such time as the Company begins to generate revenues sufficient to fund ongoing operations. The Company believes that in the aggregate, it will need as much as approximately \$5 million to \$10 million to complete this process, repay debt obligations, provide capital expenditures for additional equipment, and systems for managing the business, and cover other operating costs until revenues begin to offset our operating costs. There can be no assurances that the Company will be successful in raising the required capital to complete this portion of its business plan.

As of September 30, 2006, our working capital deficit was \$(1,062,894). Fixed assets, net of accumulated depreciation, and total assets, as of September 30, 2006 and 2005, were \$161,417 and \$190,893, respectively. Current liabilities as of September 30, 2006 were \$4,419,210.

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, revenue, results of operations, liquidity or capital expenditures.

Liquidated Damages

On May 31, 2005 we entered into a Letter Agreement (the "Letter Agreement") with the accredited investors who participated in our November 2004 private placement (the "November 2004 Investors") pursuant to which we agreed to pay to the November 2004 Investors an aggregate amount of \$120,429, representing an amount equal to 2% of the aggregate amount invested by the November 2004 Investors for each 30-day period or pro rata for any portion thereof, as liquidated damages for our failure to file a registration statement within 45 days of November 22,

17

2004 and for our failure to have such registration statement declared effective by the SEC within 90 days of November 22, 2004. The amount paid to the November 2004 Investors pursuant to the Letter Agreement represents a default of 36 days with respect to filing the registration statement and a default of 100 days with respect to having the registration statement declared effective by the SEC. Under the Letter Agreement, the liquidated damages paid to the November 2004 Investors satisfied our obligations until June 30, 2005.

From July 1, 2005 through June 30, 2006, an aggregate amount of approximately \$244,632 had accrued in liquidated damages payable to the November 2004 Investors. On March 1, 2006, we issued an aggregate principal amount \$150,000 of our 4% Unsecured Convertible Debentures and 5 year warrants to purchase an aggregate of 48,077 shares of our common stock to two of the investors in our November 2004 private placement. On June 30, 2006, we issued an aggregate principal amount \$48,248 of our 4% Unsecured Convertible Debentures and 5 year warrants to purchase an aggregate of 24,124 shares of our common stock to the final two investors in our November 2004 private placement. The debentures mature on March 1, 2008, and September 30, 2008, respectively, pay simple interest at a rate of 4% per annum and are convertible into shares of our common stock at a price equal to 1.56 per share. The warrants are exercisable into shares of our common stock at a price equal to \$1.56 per share. Our issuance of the aforementioned securities were in settlement of accrued liquidated damages which we owed to the investors for our inability to have the SEC declare our registration statement on Form SB-2 effective within the specified timeframe as set forth in the Registration Rights Agreement dated November 22, 2004. In addition, the investors agreed to forego any future accrual and payment of such

Edgar Filing: AIRTRAX INC - Form 10QSB

liquidated damages. As September 30, 2006, all damages are considered settled.

On March 17, 2006, we began to accrue liquidated damages to the investors of the first and second closings of our October 2005 private placement because we did not register shares of our common stock underlying the Series C Unsecured Convertible Debentures and common stock purchase warrants within 150 days from the initial closing date of October 18, 2005. As of September 30, 2006, an aggregate amount of approximately \$201,140 has been accrued in liquidated damages payable to the investors. We have begun discussions with the lead investor of the October 2005 private placement, and intend to engage in negotiations with the remaining investors, to settle the liquidated damages which we currently, and in the future will, owe.

RISK FACTORS

In addition to other information contained in this Form 10QSB, the following Risk Factors should be considered when evaluating the forward-looking statements contained in this Form 10-QSB:

RISKS RELATED TO OUR FINANCIAL CONDITION AND BUSINESS

WE MAY NEVER BECOME PROFITABLE AND CONTINUE AS A GOING CONCERN BECAUSE WE HAVE HAD LOSSES SINCE OUR INCEPTION.

We may never become profitable because we have incurred losses and experienced negative operating cash flow since our formation. For our three months ended September 30, 2006 and 2005, we had a net loss of approximately \$(1.0 million) and \$(3.4 million), respectively. For our fiscal years ended December 31, 2005 and 2004, we had a net loss of approximately \$(15.0 million) and \$(3.5 million), respectively. We expect to continue to incur significant expenses. Our operating expenses have been and are expected to continue to outpace revenues and result in significant losses in the near term. We anticipate that our cash requirements to fund operating or investing cash requirements over the next 6 months will be greater than our current cash on hand. We may never be able to reduce these losses, which will require us to seek additional debt or equity financing. While we are in discussions with several prospective lenders, we do not currently have commitments for additional funds and there can be no assurance that additional financing will be available, or if available, will be on acceptable terms. If we are unable to obtain sufficient funds during the next 6 months we will further reduce the size of our organization and may be forced to reduce and/or curtail our production and operations, all of which could have a material adverse impact on our business prospects.

WE HAVE A LIMITED OPERATING HISTORY

We have been in operation since 1995. However, since 1995, our operations have been limited to the development of our Omni-Directional products, and limited revenue has been generated during this period. Consequently, our business may be subject to the many risks and pitfalls commonly experienced by companies with limited operations.

18

OUR BUSINESS OPERATIONS WILL BE HARMED IF WE ARE UNABLE TO OBTAIN ADDITIONAL FUNDING.

Our business operations will be harmed if we are unable to obtain additional funding. We do not know if additional financing will be available when needed, or if it is available, if it will be available on acceptable terms. Insufficient funds may prevent us from implementing our business strategy or may require us to delay, scale back or eliminate certain opportunities for the provision of our

Edgar Filing: AIRTRAX INC - Form 10QSB

technology and products. As of September 30, 2006, we have loaned \$6,275,881 to Filco.

On January 20, 2006, Filco filed for insolvency in Germany and a receiver was appointed. As a result, on February 7, 2006, the Company terminated the tentative agreement to acquire Filco stock and began negotiations with the receiver to acquire some or all of the Filco assets. The \$6,275,881 of advances to Filco that were outstanding at December 31, 2005, were secured by liens filed against the machinery and equipment owned by Filco which in 2003 was appraised at \$5,400,000, and by liens filed against its intellectual property, which had not been appraised. Due to the uncertainty of the Company's position under German bankruptcy law, \$4,275,881 of the Filco advances were written off in 2005, and the remaining \$2,000,000 was written off in 2006. In addition, \$413,174 of Company inventory stored at the Filco plant was abandoned and written off during 2006. During 2006, an auction of Filco assets was conducted by the receiver who did not acknowledge the Airtrax liens against property and equipment.

THE PRICING POLICY FOR OUR LIFT TRUCKS MAY BE SUBJECT TO CHANGE, AND ACTUAL SALES OR OPERATING MARGINS MAY BE LESS THAN PROJECTED.

We are assessing present and projected component pricing in order to establish a pricing policy for the SIDEWINDER Lift Truck. We have not finalized our assessment as current prices for certain lift truck components reflect special development charges, which are expected to be reduced as order volume for such components increase and as manufacturing efficiencies improve. We intend to price our lift trucks so as to maximize sales yet provide sufficient operating margins. Given the uniqueness of our product, we have not yet established final pricing sensitivity in the market. Consequently, the pricing policy for its lift trucks may be subject to change, and actual sales or operating margins may be less than projected.

WE HAVE RECEIVED LIMITED INDICATIONS OF THE COMMERCIAL ACCEPTABILITY OF OUR OMNI-DIRECTIONAL LIFT TRUCK. ACCORDINGLY, WE CANNOT PREDICT WHETHER OUR OMNI-DIRECTIONAL PRODUCTS CAN BE MARKETED AND SOLD IN A COMMERCIAL MANNER.

Our success will be dependent upon our ability to sell Omni-Directional products in quantities sufficient to yield profitable results. To date, we have received limited indications of the commercial acceptability of our Omni-Directional lift truck. Accordingly, we cannot predict whether the Omni-Directional product can be marketed and sold in a commercial manner.

WE CANNOT ASSURE THAT WE WILL HAVE IN PLACE PATENT PROTECTION AND CONFIDENTIALITY AGREEMENTS FOR OUR PROPRIETARY TECHNOLOGY. IF WE DO NOT ADEQUATELY PROTECT OUR INTELLECTUAL PROPERTY RIGHTS, THERE IS A RISK THAT THEY WILL BE INFRINGED UPON OR THAT OUR TECHNOLOGY INFRINGES UPON ONE OF OUR COMPETITOR'S PATENTS. AS A RESULT, WE MAY EXPERIENCE A LOSS OF REVENUE AND OUR OPERATIONS MAY BE MATERIALLY HARMED.

Our success will be dependent, in part, upon the protection of our proprietary Omni-Directional technology from competitive use. A form of our Omni-Directional technology was originally patented in 1973 and was sold to the US Navy. We secured a transfer of this technology from the Navy in 1996 under the terms of a CRADA agreement (Cooperative Research and Development Agreement) and we have worked since that time to commercialize Omni-Directional products. We received 3 patents regarding the "redesign" of the wheel. In addition, we have a license agreements for the algorithms used to control vehicular movement, and a patent for this technology has been applied for. Further, we have applied for patents for a movable operator's control station and a munitions handler. Notwithstanding the foregoing, we believe our lack of patent protection is a material competitive risk. Our competitors could reverse engineer our technology

to build similar products. Also, certain variations to the technology could be made whereby our competitors may use the technology without infringing upon our intellectual property. The patent for the Omni-Directional wheel expired in 1990. We, however, have received patent protection of certain other aspects of its Omni-Directional wheel, and for features specific to our lift truck. In addition to the patent applications, we rely on a combination of trade secrets, nondisclosure agreements and other contractual provisions to protect our intellectual property rights. Nevertheless, these measures may be inadequate to safeguard our underlying technology. If these measures do not protect the intellectual property rights, third parties could use our technology, and our ability to compete in the market would be reduced significantly. In addition, if the sale of our product extends to foreign countries, we may not be able to effectively protect its intellectual property rights in such foreign countries.

In the future, we may be required to protect or enforce our patents and patent rights through patent litigation against third parties, such as infringement suits or interference proceedings. These lawsuits could be expensive, take significant time, and could divert management's attention from other business concerns. These actions could put our patents at risk of being invalidated or interpreted narrowly, and any patent applications at risk of not issuing. In defense of any such action, these third parties may assert claims against us. We cannot provide any assurance that we will have sufficient funds to vigorously prosecute any patent litigation, that we will prevail in any of these suits, or that the damages or other remedies awarded, if any, will be commercially valuable. During the course of these suits, there may be public announcements of the results of hearings, motions and other interim proceedings or developments in the litigation. If securities analysts or investors perceive any of these results to be negative, it could cause the price of our common stock to decline.

WE CURRENTLY LACK ESTABLISHED DISTRIBUTION CHANNELS FOR OUR LIFT TRUCK PRODUCT LINE.

We do not have an established channel of distribution for our lift truck product line. We have initiated efforts to establish a network of designated dealers throughout the United States. Although we have received indications of interest from a number of equipment distributors, to date, such indications have been limited. We cannot predict whether we will be successful in establishing our intended dealer network.

IF WE ARE UNABLE TO RETAIN THE SERVICES OF ROBERT WATSON, OUR CHIEF EXECUTIVE OFFICER, OR IF WE ARE UNABLE TO SUCCESSFULLY RECRUIT, QUALIFIED PERSONNEL, WE MAY NOT BE ABLE TO CONTINUE OPERATIONS.

Our ability to successfully conduct our business affairs will be dependent upon the capabilities and business acumen of current management including Robert Watson, our President and Chief Executive Officer. We have not entered into an employment agreement with Mr. Watson and do not maintain key man life insurance with respect to Mr. Watson. Accordingly, shareholders must be willing to entrust all aspects of our business affairs to our current management. Further, the loss of any one of our management team could have a material adverse impact on our continued operation.

OUR INDUSTRY AND PRODUCTS ARE CONSIDERED TO BE HIGH-RISK WITH A HIGH INCIDENCE OF SERIES PERSONAL INJURY OR PROPERTY LOSS WHICH COULD HAVE A MATERIAL ADVERSE IMPACT ON OUR BUSINESS.

The manufacture, sale and use of Omni-Directional lift trucks and other mobility or material handling equipment is generally considered to be an industry of a

Edgar Filing: AIRTRAX INC - Form 10QSB

high risk with a high incidence of serious personal injury or property loss. In addition, although we intend to provide on-site safety demonstrations, the unique, sideways movement of the lift truck may heighten potential safety risks. Despite the fact that we intend to maintain sufficient liability insurance for the manufacture and use of our products, one or more incidents of personal injury or property loss resulting from the operation of our products could have a material adverse impact on our business.

IF WE DO NOT SUCCESSFULLY DISTINGUISH AND COMMERCIALIZE OUR DEVELOPED PROPRIETARY PRODUCTS AND SERVICES, WE WILL NOT ATTRACT A SUFFICIENT NUMBER OF CUSTOMERS. ACCORDINGLY, WE MAY BE UNABLE TO COMPETE SUCCESSFULLY WITH OUR COMPETITORS OR TO GENERATE REVENUE SIGNIFICANT TO SUSTAIN OUR OPERATIONS.

Although management believes our product will have significant competitive advantages to conventional lift trucks, we are competing in an industry populated by some of the foremost equipment and vehicle manufacturers in the

20

world. All of these companies have greater financial, engineering and other resources than us. No assurances can be given that any advances or developments made by such companies will not supersede the competitive advantages of our Omni-Directional lift truck. In addition, many of our competitors have long-standing arrangements with equipment distributors and carry one or more of competitive products in addition to lift trucks. These distributors are prospective dealers for our company. It therefore is conceivable that some distributors may be loath to enter into any relationships with us for fear of jeopardizing existing relationships with one or more competitors.

RISKS RELATING TO OUR COMMON STOCK

WE HAVE ISSUED COMMON STOCK, WARRANTS, AND CONVERTIBLE NOTES TO INVESTORS AND IN EXCHANGE FOR FEES AND SERVICES AT A DISCOUNT TO THE MARKET PRICE OF OUR COMMON STOCK AT THE TIME OF SUCH ISSUANCE. THIS RESULTS IN A LARGE NUMBER OF SHARES WHICH HAVE BEEN ISSUED AND A LARGE NUMBER OF SHARES UNDERLYING OUR WARRANTS AND OTHER CONVERTIBLE SECURITIES THAT ARE OR MAY BE AVAILABLE FOR FUTURE SALE AND THE SALE OF THESE SHARES MAY DEPRESS THE MARKET PRICE OF OUR COMMON STOCK.

We had 24,015,019 shares of common stock outstanding as of November 10, 2006, and we had convertible notes which require the issuance of 1,537,820 additional shares of common stock pursuant to our May and October 2005 private placements and 2006 Note issuances, and warrants which require the issuance of 5,628,988 additional shares of common stock pursuant to our November 2004, and February, May, and October 2005 private placements 2006 note issuances, each of which have been issued or which are to be issued upon conversion or exercise to investors of our company at a discount to the market price of our common stock at the time of such issuance.. Further, we often issue common stock and warrants in exchange for fees and services at a discount to the market price of our common stock at the time of such issuance. This results in a large number of shares, which have been issued, a large number of shares underlying our warrants and other convertible securities that are or may be available for future sale, and may create an overhang of securities for sale. The sale of these shares which were or will be issued upon exercise or conversion of our securities at a discount to the market price of our common stock at the time of issuance may depress the market price of our common stock and is dilutive to shareholder value.

OUR COMMON STOCK IS SUBJECT TO THE "PENNY STOCK" RULES OF THE SEC AND THE TRADING MARKET IN OUR SECURITIES IS LIMITED, WHICH MAKES TRANSACTIONS IN OUR STOCK CUMBERSOME AND MAY REDUCE THE VALUE OF AN INVESTMENT IN OUR STOCK.

The Securities and Exchange Commission has adopted Rule 15g-9 which establishes

Edgar Filing: AIRTRAX INC - Form 10QSB

the definition of a "penny stock," for the purposes relevant to us, as any equity security that has a market price of less than \$5.00 per share or with an exercise price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, the rules require:

- o that a broker or dealer approve a person's account for transactions in penny stocks; and

- o the broker or dealer receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased.

In order to approve a person's account for transactions in penny stocks, the broker or dealer must:

- o obtain financial information and investment experience objectives of the person; and

- o make a reasonable determination that the transactions in penny stocks are suitable for that person and the person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks.

The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule prescribed by the Commission relating to the penny stock market, which, in highlight form:

- o sets forth the basis on which the broker or dealer made the suitability determination; and

21

- o that the broker or dealer received a signed, written agreement from the investor prior to the transaction.

Generally, brokers may be less willing to execute transactions in securities subject to the "penny stock" rules. This may make it more difficult for investors to dispose of our common stock and cause a decline in the market value of our stock.

Disclosure also has to be made about the risks of investing in penny stocks in both public offerings and in secondary trading and about the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and the rights and remedies available to an investor in cases of fraud in penny stock transactions. Finally, monthly statements have to be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

Item 3. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. Based on an evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended) required by paragraph (b) of Rule 13a-15 or Rule 15d-15, as of September 30, 2006, our Chief Executive Officer and Acting Chief Financial Officer has concluded that our disclosure controls and procedures were effective in ensuring 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. Our Chief Executive Officer and Acting Chief Financial Officer also concluded that, as of September 30, 2006, our disclosure controls and procedures were effective in ensuring that

Edgar Filing: AIRTRAX INC - Form 10QSB

information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Acting Chief Financial Officer, to allow timely decisions regarding required disclosure.

(b) Changes in Internal Controls. During the quarter ended September 30, 2006, there were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

22

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the nine months ended September 30, 2006, the Company issued 670,963 shares of common stock were issued for services and recorded expenses in the amount of \$1,325,264.

During the quarter ended September 30, 2006, holders converted \$819,800 of convertible debt, along with accrued interest into stock, resulting in the issuance of 534,352 shares of common stock.

During the quarter ended September 30, 2006, a holder converted \$253,303 of convertible debt and accrued interest to stock, resulting in the issuance of 235,575 shares.

On July 26, 2006, the Company issued a 12% Series A Convertible Note in the principal amount of \$400,000, together with warrants to purchase 282,052 shares of common stock to a qualified institutional buyer. The Note is convertible into shares of common stock at a price equal to \$1.56 per share. In addition, all principal and accrued and unpaid interest was due on October 20, 2006. The Company did not repay the note in the amount of \$412,000, inclusive of principal and accrued and unpaid interest, on or prior to October 20, 2006. The Company is currently in negotiations with the holder to repay the note through the payment of cash, or issuance of shares of common stock, or a combination of both.

* All of the above offerings and sales were deemed to be exempt under rule 506 of Regulation D and Section 4(2) of the Securities Act of 1933, as amended. No advertising or general solicitation was employed in offering the securities. The offerings and sales were made to a limited number of persons, all of whom were accredited investors, business associates of Airtrax or executive officers of Airtrax, and transfer was restricted by Airtrax in accordance with the requirements of the Securities Act of 1933. In addition to representations by the above-referenced persons, we have made independent determinations that all of the above-referenced persons were accredited or sophisticated investors, and that they were capable of analyzing the merits and risks of their investment, and that they understood the speculative nature of their investment. Furthermore, all of the above-referenced persons were provided with access to our Securities and Exchange Commission filings.

Item 3. Defaults Upon Senior Securities

The Company is currently in default on its 12% Series A Convertible Note in the

Edgar Filing: AIRTRAX INC - Form 10QSB

principal amount of \$400,000 which the Company issued to a qualified institutional buyer on July 26, 2006. All principal and accrued and unpaid interest was due on October 20, 2006. The Company did not repay the note in the amount of \$412,000, inclusive of principal and accrued and unpaid interest, on or prior to October 20, 2006. The Company is currently in negotiations with the holder to repay the note through the payment of cash, or issuance of shares of common stock, or a combination of both. As of this report, the Company is negotiating the following proposed settlement:

- o Payment of outstanding interest, approx. \$14,000;
- o Partial payment of principal;
- o 75,000 shares of stock per default provisions;
- o Default interest rate prospectively 18%; and
- o Monthly interest payments and an extension fee.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

23

Item 6. Exhibits

(a) Exhibits.

31.1 Certification by Chief Executive Officer and Acting Chief Financial Officer pursuant to Sarbanes-Oxley Section 302 (filed herewith).

32.1 Certification by Chief Executive Officer and Acting Chief Financial Officer pursuant to 18 U.S.C. Section 1350 (filed herewith).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AIRTRAX, INC.

By: /s/ Robert Watson

Robert Watson, President,
Chief Executive Officer, and Acting
Chief Financial Officer

November 20, 2006

24