SOLITRON DEVICES INC
Form 10-Q
October 15, 2008

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

FORM 10-Q

(Mark one)

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

For the quarterly period ended August 31, 2008

or

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _______ to _______

Commission File No. 1-4978

SOLITRON DEVICES, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	22-1684144 (I.R.S. Employer Identification No.)
3301 Electronics Way, West Palm Beach, Florida (Address of Principal Executive Offices)	33407 (zip code)

(561) 848-4311
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller reporting company x

The number of shares of the registrant's common stock, $0.01 par value, outstanding as of October 9,2008 was 2,262,904.

SOLITRON DEVICES, INC.

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SOLITRON DEVICES, INC.
CONDENSED BALANCE SHEETS
(Unaudited, in thousands)

	August 31, 2008	Feb 29, 2008
ASSETS		
CURRENT ASSETS :		
Cash	$ 76	$ 75
Investment in treasury bills	4,979	4,410
Accounts receivable, less allowance for doubtful accounts of $7	783	1,026
Inventories, net	2,580	2,985
Prepaid expenses and other current assets	140	104
TOTAL CURRENT ASSETS	8,558	8,600
PROPERTY, PLANT AND EQUIPMENT, net	558	562
OTHER ASSETS	240	245
TOTAL ASSETS	$ 9,356	$ 9,407
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable – Post-petition	$ 314	$ 529
Accounts payable – Pre-petition, current portion	1,100	1,114
Customer deposit	256	387
Accrued expenses and other current liabilities	377	554
TOTAL CURRENT LIABILITIES	2,047	2,584
LONG TERM LIABILITIES, net of current portion	345	345
TOTAL LIABILITIES	2,392	2,929
COMMITMENTS & CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Preferred stock, $.01 par value, authorized 500,000 shares, none issued	-0-	-0-
Common stock, $.01 par value, authorized 10,000,000 shares, 2,262,904 shares issued and outstanding, net of 173,287 shares of treasury stock	23	23
Additional paid-in capital	2,733	2,733
Retained earnings	4,208	3,722
TOTAL STOCKHOLDERS' EQUITY	6,964	6,478
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 9,356	$ 9,407

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

SOLITRON DEVICES, INC.
CONDENSED STATEMENTS OF INCOME
THREE AND SIX MONTHS ENDED AUGUST 31,
(Unaudited, in thousands except for share and per share amounts)

	Three Months 2008	Three Months 2007	Six Months 2008	Six Months 2007
NET SALES	$ 2,071	$ 1,847	$ 4,240	$ 3,590
Cost of Sales	1,649	1,551	3,272	2,921
Gross Profit	422	296	968	669
Selling, General and Administrative Expenses	233	235	517	505
Operating Income/(Loss)	189	61	451	164
OTHER INCOME				
Other Income, Net	-	(3)	-	1
Interest Income	25	46	35	90
Interest Expense	-	-	-	-
Other Income, Net	25	43	35	91
Net Income/(Loss)	$ 214	$ 104	$ 486	$ 255
INCOME/(LOSS) PER SHARE : Basic	$ .09	$ .05	$ .21	$ .11
: Diluted	$ .09	$ .04	$ .20	$ .10
WEIGHTED AVERAGE				
SHARES OUTSTANDING : Basic	2,262,904	2,263,046	2,262,904	2,263,046
: Diluted	2,474,926	2,445,446	2,476,949	2,441,395

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

SOLITRON DEVICES, INC.
CONDENSED STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED AUGUST 31,
(Unaudited, in thousands)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (Loss)/Income	$ 486	$ 255
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	98	94
Changes in operating assets and liabilities:		
(Increase) Decrease in:		
Investment in treasury bills	(569)	(461)
Accounts receivable	243	(46)
Inventories	405	40
Prepaid expenses and other current assets	(36)	(2)
Other non-current assets	5	(207)
Increase (Decrease) in:		
Accounts payable - Post-petition	(215)	168
Accounts payable - Pre-petition	(14)	(14)
Customer deposit	(131)	-
Accrued expenses and other current liabilities	(177)	(80)
Other non-current liabilities	-	187
NET CASH PROVIDED BY OPERATING ACTIVITIES	95	(66)
CASH FLOW FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(94)	(54)
NET CASH (USED IN) INVESTING ACTIVITIES	(94)	(54)
CASH FLOW FROM FINANCING ACTIVITIES:		
Exercise of stock options	-	-
NET CASH FROM FINANCING ACTIVITIES	-	-
NET INCREASE/(DECREASE) IN CASH	1	(120)
CASH AT THE BEGINNING OF PERIOD	75	163
CASH AT THE END OF PERIOD	$ 76	$ 43

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

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

1. GENERAL AND SIGNIFICANT ACCOUNTING POLICIES:

GENERAL:

The financial information included herein is unaudited; however, such information reflects all adjustments (consisting primarily of normal recurring adjustments), which are, in the opinion of management, necessary for a fair statement of the results for the interim period.

The accompanying unaudited interim condensed financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission for reporting on Form 10-Q. Pursuant to such rules and regulations, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted.

The information contained in this Quarterly Report on Form 10-Q should be read in conjunction with the Notes to the Consolidated Financial Statements appearing in the Solitron Devices, Inc. Annual Report on Form 10-K for the year ended February 29, 2008.

The results of operations for the six-month period ended August 31, 2008 are not necessarily indicative of the results to be expected for the entire year ending February 28, 2009.

SIGNIFICANT ACCOUNTING POLICIES:

Cash
Cash includes demand deposits and money market accounts. The Company has $76,000 in cash deposits which is $24,000 under the $100,000 limit for FDIC insurance.

Investment in Treasury Bills
During the first quarter of this fiscal year Company management decided to reclassify its investment in treasury bills from cash and cash equivalents and report it separately as “Investment in Treasury Bills”. Investment in Treasury Bills includes treasury bills with maturities of one year or less and is stated at market value. The corresponding amount of cash and cash equivalents shown on the prior period balance sheet and statement of cash flows has been reclassified to reflect this change in accounting principle (see footnote 11).

Accounts Receivable
The Company extends unsecured credit to its customers in the ordinary course of business but mitigates the associated credit risk by performing credit checks and actively pursuing past due accounts. An allowance for doubtful accounts has been established. The allowance amount was $7,000 as of August 31, 2008. The Company has not had a bad debt in the past two years.

Shipping and Handling
Shipping and handling costs billed to customers are recorded in net sales. Shipping costs incurred by the Company are recorded in cost of sales.

Inventories
Inventories are stated at the lower of cost or market. Cost is determined using the “first-in, first-out” (FIFO) method. The Company buys raw material only to fill customer orders. Excess raw material is created only when a vendor

imposes a minimum buy in excess of actual requirements. Such excess material will usually be utilized to meet the requirements of the customer's subsequent orders. If excess material is not utilized after two fiscal years it is fully reserved.

The Company's inventory valuation policy is as follows:

Raw material /Work in process:	All material purchased, processed and/or used in the last two fiscal years is valued at the lower of its acquisition cost or market. All material not purchased/used in the last two fiscal years is fully reserved for.

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

Finished goods:	All finished goods with firm orders for later delivery are valued (material and overhead) at the lower or cost or market. All finished goods with no orders are fully reserved.
Direct labor costs:	Direct labor costs are allocated to finished goods and work in process inventory based on engineering estimates of the amount of man hours required from the different direct labor departments to bring each device to its particular level of completion.

Stock Based Compensation

In December 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure, and amendment of FASB Statement No. 123". This statement amends SFAS No. 123, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. This statement also amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has prepared its interim financial statements for the quarters ended August 31, 2008 and August 31, 2007 in accordance with SFAS No. 148.

During the quarters ended August 31, 2008 and August 31, 2007, the Company did not issue any stock-based compensation to its employees or directors.

2. ENVIRONMENTAL REGULATION:

While the Company believes that it has the environmental permits necessary to conduct its business and that its operations conform to present environmental regulations, increased public attention has been focused on the environmental impact of semiconductor manufacturing operations. The Company, in the conduct of its manufacturing operations, has handled and does handle materials that are considered hazardous, toxic or volatile under federal, state and local laws and, therefore, is subject to regulations related to their use, storage, discharge and disposal. No assurance can be made that the risk of accidental release of such materials can be completely eliminated. In the event of a violation of environmental laws, the Company could be held liable for damages and the costs of remediation. In addition, the Company, along with the rest of the semiconductor industry, is subject to variable interpretations and governmental priorities concerning environmental laws and regulations. Environmental statutes have been interpreted to provide for joint and several liability and strict liability regardless of actual fault. There can be no assurance that the Company will not be required to incur costs to comply with, or that the operations, business or financial condition of the Company will not be materially adversely affected by current or future environmental laws or regulations.

3. ENVIRONMENTAL LIABILITIES:

The Company entered into an Ability to Pay Multi-Site Settlement Agreement with the United States Environmental Protection Agency ("USEPA"), effective February 24, 2006 ("Settlement Agreement"), to resolve the Company's alleged liability to USEPA at the following sites: Solitron Microwave Superfund Site, Port Salerno, Florida ("Port Salerno Site"); Petroleum Products Corporation Superfund Site, Pembroke Park, Florida; Casmalia Resources Superfund Site, Santa Barbara, California "(Casmalia Site"); Solitron Devices Site, Riviera Beach, Florida (the "Riviera Beach Site"); and City Industries Superfund Site, Orlando, Florida (collectively, the "Sites"). The Settlement Agreement required the Company to pay to USEPA the sum of $74,000 by February 24, 2008; the Company paid the entire sum of $74,000 to

USEPA on February 27, 2006. In addition, the Company is required to pay to USEPA the sum of $10,000 or 5% of Solitron's net after-tax income over the first $500,000, if any, whichever is greater, for each year from 2008-2012. For payment to USEPA to be above $10,000 for any of these five years, the Company's net income must exceed $700,000 for such year, which has happened in fiscal year 2001, fiscal year 2006, and fiscal year 2008. The Company accrued $50,000 for its remaining obligations under the Settlement Agreement.

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

In consideration of the payments made by the Company under the Settlement Agreement, USEPA agreed not to sue or take any administrative action against the Company with regard to any of the Sites. The Company has also been notified by a group of alleged responsible parties formed at the Casmalia Site ("Casmalia PRP Group") that, based on their review and lack of objection to the Settlement Agreement, the Casmalia PRP Group does not anticipate pursuing Solitron for cost recovery at the Casmalia site.

On October 21, 1993, a Consent Final Judgment was entered into between the Company and the Florida Department of Environmental Protection ("FDEP") in the Circuit Court of the Nineteenth Judicial Circuit of Florida in and for Martin County, Florida, in Case No. 91-1232 CA (the "Consent Final Judgment"). The Consent Final Judgment required the Company to remediate the Port Salerno and Riviera Beach Sites, make monthly payments to escrow accounts for each Site until the sale of the Sites to fund the remediation work, take all reasonable steps to sell the two Sites and, upon the sale of the Sites, apply the net proceeds from the sales to fund the remediation work. Both Sites have been sold pursuant to purchase agreements approved by FDEP.

Prior to the sale of the Port Salerno Site and Riviera Beach Site, USEPA took over from FDEP as the lead regulatory agency for the remediation of the Sites. At the closing of the sale of each Site, the net proceeds of sale were distributed to USEPA and/or FDEP or other parties, as directed by the agencies. In addition, upon the sale of the Riviera Beach Site, the Riviera Beach Escrow Account was transferred to USEPA, as directed by the agencies. The current balance in the Port Salerno Escrow Account is approximately $58,000. At present, work at the Port Salerno Site is being performed by USEPA. Work at the Riviera Beach Site is being performed by Honeywell, Inc. ("Honeywell"), pursuant to an Administrative Order on Consent entered into between Honeywell and USEPA. The Company has been notified by FDEP that the successful performance of remediation work in accordance with the Consent Final Judgment standards by USEPA at the Port Salerno Site and by Honeywell at the Riviera Beach Site will be construed by FDEP as discharging the Company's remediation obligations under the Consent Final Judgment.

There remains a possibility that FDEP will determine at some time in the future that the final remedy approved by USEPA and implemented at either, or both of, the Port Salerno Site and Riviera Beach Site does not meet the State cleanup requirements imposed by the Consent Final Judgment. If such a final determination is made by FDEP, there is a possibility that FDEP will require the Company to implement additional remedial action at either, or both of, the Port Salerno Site and Riviera Beach Site.

By letter dated November 16, 2006, FDEP notified the Company that FDEP has unreimbursed expenses associated with the Port Salerno Site and Riviera Beach Site of $214,800. FDEP further notified the Company that FDEP required the Company to resume payments under Consent Final Judgment to ensure that there are adequate funds to cover FDEP's unreimbursed expenses and the Company's residual liability under the Consent Final Judgment. During a follow up telephone conversation with the Company's attorney, FDEP advised the Company that FDEP will prepare a justification for the asserted unreimbursed expenses. Upon receipt of the cost reimbursement package, the Company is required to transfer $55,000.00 from the Port Salerno Escrow Account to FDEP as partial payment for FDEP's unreimbursed expenses that are otherwise recoverable under the Consent Final Judgment. FDEP further stated, during the telephone conversation, that FDEP will work with the Company to establish a reduced payment schedule for the Company to resume under the Consent Final Judgment based on an appropriate showing by the Company of financial hardship. The Company is currently awaiting receipt of FDEP's cost reimbursement package. Upon receipt of that documentation, the Company will be required to provide a recommendation to FDEP for resumption of payments to FDEP under the Consent Final Judgment based on the Company's present ability to pay.

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

On August 7, 2002, the Company received a Request for Information from the State of New York Department of Environmental Conservation ("NYDEC"), seeking information on whether the Company had disposed of certain wastes at the Clarkstown Landfill Site located in the Town of Clarkstown, Rockland County, New York (The Clarkstown Landfill Site"). By letter dated August 29, 2002, the Company responded to the Request for Information and advised NYDEC that the Company's former Tappan, New York facility had closed in the mid-1980's, prior to the initiation of the Company's bankruptcy proceedings described below. The Company contends that, to the extent that NYDEC has a claim against the Company as a result of the Company's alleged disposal of wastes at the Clarkstown Landfill Site prior to the closing of the Company's former Tappan facility in the mid-1980's, the claim was discharged in bankruptcy as a result of the Bankruptcy Court's August 1993 Order. At NYDEC's request, the Company entered into a revised Tolling Agreement with NYDEC on October 7, 2008, which provides for the tolling of applicable statutes of limitation through the earlier of June 26, 2009, or the date the State institutes a suit against the Company for any claims associated with the Clarkstown Landfill Site. It is not known at this time whether NYDEC will pursue a claim against the Company in connection with the Clarkstown Landfill Site. As of the date of this filing, no such claim has been made.

4. EARNINGS PER SHARE:

The shares used in the computation of the Company's basic and diluted earnings per common share were as follows:

	For the three months ended August 31,		For the six months ended August 31,	
	2008	2007	2008	2007
Weighted average common shares outstanding	2,262,904	2,263,046	2,262,904	2,263,046
Dilutive effect of employee stock options	212,022	182,400	214,045	178,349
Weighted average common shares outstanding, assuming dilution	2,474,926	2,445,446	2,476,949	2,441,395

Weighted average common shares outstanding, assuming dilution, include the incremental shares that would be issued upon the assumed exercise of stock options. For the three month periods ended August 31, 2008 and August 31, 2007, 13,800 of the Company's stock options were excluded from the calculation of diluted earning per share because the exercise prices of the stock options were greater than or equal to the average price of the common shares, and therefore their inclusion would have been anti-dilutive.

5. INVENTORIES:

As of August 31, 2008, inventories consist of the following:

	Gross	Reserve	Net
Raw Materials	$ 1,431,000	$ (321,000)	$ 1,110,000
Work-In-Process	1,989,000	(552,000)	1,437,000
Finished Goods	469,000	(436,000)	33,000
Totals	$ 3,889,000	$ (1,309,000)	$ 2,580,000

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

6. INCOME TAXES:

At August 31, 2008, the Company has net operating loss carryforwards of approximately $12,598,000 that expire through 2022. Such net operating losses are available to offset future taxable income, if any. As the utilization of such net operating losses for tax purposes is not assured, the deferred tax asset has been mostly reserved through the recording of a 90% valuation allowance. Should a cumulative change in the ownership of more than 50% occur within a three-year period, there could be an annual limitation on the use of the net operating loss carryforward.

Total net deferred taxes are comprised of the following at August 31, 2008:

Deferred tax assets:		
Loss carryforwards	$	4,542,000
Allowance for doubtful accounts		3,000
Inventory allowance		3,565,000
Accrued bonuses		77,000
Section 263A capitalized costs		1,111,000
Total deferred tax assets		9,298,000
Valuation allowance		(8,833,000)
Net deferred tax assets		465,000
Deferred tax liabilities:		
Depreciation		278,000
Total deferred tax liabilities		278,000
Total net deferred taxes	$	187,000

The change in the valuation allowance on deferred tax assets is due principally to the utilization of the net operating loss for the quarter ending August 31, 2008.

A reconciliation of the provision for income taxes to the amount calculated using the statutory federal rate (34%) for quarter ending August 31, 2008, is as follows:

		2008		2007
Income Tax Provision at				
U.S. Statutory Rate	$	272,000	$	147,000
State Taxes, Net of Federal Benefit		29,000		16,000
Alternative Minimum Taxes		-		-
Utilization of Net Operating Loss Carryforward		(301,000)		(163,000)
Income Tax Provision	$	-	$	-

The Company paid $8,000 in federal and state alternative minimum taxes for fiscal year 2007 and has accrued $11,000 in federal and state alternative minimum taxes for fiscal year 2008.

7. OTHER INCOME:

The $25,000 of other income reflected in the condensed statements of income for the quarter ended August 31, 2008 consists entirely of interest income on investment in treasury bills net of changes in market value. For the fiscal quarter ended August 31, 2007, the Company earned $43,000 of other income consisting of $46,000 interest income on investment in treasury bills net of changes in market value less $3,000 of other expense due to the loss of an equipment deposit because of non-delivery by the vendor.

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

8. ACCRUED EXPENSES:

As of August 31, 2008 accrued expenses and other liabilities consisted of the following:

Payroll and related employee benefits	$ 318,000
Other liabilities	59,000
	$ 377,000

9. EXPORT SALES AND MAJOR CUSTOMERS:

Revenues from domestic and export sales to unaffiliated customers for the three months ended August 31, 2008 are as follows:

Geographic Region	Power Transistors	Hybrids	Field Effect Transistors	Power MOSFETS	Totals
Europe and Australia	$ 32,000	$ 184,000	$ 10,000	$ 0	$ 226,000
Canada and Latin America	0	0	5,000	15,000	20,000
Far East and Middle East	0	0	3,000	20,000	23,000
United States	297,000	1,015,000	155,000	335,000	1,802,000
Totals	$ 329,000	$ 1,199,000	$ 173,000	$ 370,000	$ 2,071,000

Revenues from domestic and export sales to unaffiliated customers for the three months ended August 31, 2007 are as follows:

Geographic Region	Power Transistors	Hybrids	Field Effect Transistors	Power MOSFETS	Totals
Europe and Australia	$ 4,000	$ 137,000	$ 22,000	$ 0	$ 163,000
Canada and Latin America	16,000	0	0	0	16,000
Far East and Middle East	6,000	0	0	44,000	50,000
United States	277,000	907,000	183,000	251,000	1,618,000
Totals	$ 303,000	$ 1,044,000	$ 205,000	$ 295,000	$ 1,847,000

Revenues from domestic and export sales are attributed to global geographic region according to the location of the customer’s primary manufacturing or operating facilities.

Sales to the Company's top two customers, Raytheon Company and the U.S. Government, accounted for approximately 50% of net sales for the quarter ended August 31, 2008 as compared with 44% of the Company's net sales for the quarter ended August 31, 2007. Sales to Raytheon Company accounted for approximately 39% of net sales for the quarter ended August 31, 2008 and 34% for the quarter ended August 31, 2007. Sales to the U.S. Government accounted for approximately 11% of net sales for the quarter ended August 31, 2008 and 10% for the quarter ended August 31, 2007.

10. Major Suppliers

Purchases from the Company’s two top suppliers, Platronics Seals and Egide USA Inc., accounted for approximately 19% of total purchases of production materials for the quarter ended August 31, 2008. For the quarter ended August

31, 2007, purchases from the Company’s two top suppliers, CPS Technologies, Inc. and Coining Inc., accounted for approximately 14% of the Company's total purchases of production materials.

SOLITRON DEVICES, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

11. Change in accounting principle

During the first quarter of this fiscal year Company management decided to remove its investment in treasury bills from cash and cash equivalents and report it separately as "Investment in Treasury Bills". Investment in Treasury Bills includes treasury bills with maturities of one year or less and is stated at market value. The Company has reclassified its February 29, 2008 balance sheet to reflect this change in accounting principle. The reclassification is as follows:

Before change:		
Cash and cash equivalents	$	4,485,000
After change:		
Cash	$	75,000
Investment in treasury bills		4,410,000
As of August 31, 2008:		
Cash	$	76,000
Investment in treasury bills		4,979,000

Income from treasury bill investments will include both accrued interest income and differences between accrued surrender value and market value.

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

Overview:

Solitron Devices, Inc., a Delaware corporation (the "Company" or "Solitron"), designs, develops, manufactures and markets solid-state semiconductor components and related devices primarily for the military and aerospace markets. The Company manufactures a large variety of bipolar and metal oxide semiconductor ("MOS") power transistors, power and control hybrids, junction and power MOS field effect transistors and other related products. Most of the Company's products are custom made pursuant to contracts with customers whose end products are sold to the U.S. Government. Other products, such as Joint Army/Navy transistors, diodes and Standard Military Drawings voltage regulators, are sold as standard or catalog items.

The following discussion and analysis of factors which have affected the Company's financial position and operating results during the periods included in the accompanying condensed financial statements should be read in conjunction with the Financial Statements and the related Notes to Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended February 29, 2008 and the Condensed Financial Statements and the related Notes to the Condensed Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q.

Significant Accounting Policies:

The discussion and analysis of our financial condition and results of operations are based upon the condensed financial statements included elsewhere in this Quarterly Report on Form 10-Q which are prepared in accordance with accounting principles generally accepted in the United States. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. These estimates and assumptions are affected by management's application of accounting policies. Our critical accounting policies include inventories, valuation of plant, equipment, revenue recognition and accounting for income taxes. A discussion of all of these critical accounting policies can be found in Note 1 of the "Notes To Financial Statements" in Item 8 of our Annual Report on Form 10-K for the fiscal year ended February 29, 2008.

Trends and Uncertainties:

During the three months ended August 31, 2008 the Company's book-to-bill ratio was approximately 1.44 as compared to approximately 1.48 for the three months ended August 31, 2007, reflecting a slight decrease in the volume of orders booked. The Company does not believe that the quarter-to-quarter change in the book-to-bill ratio indicates a specific trend in the demand for the Company's products. Generally, the intake of orders varies greatly as a result of the fluctuations in the general economy, variations in defense spending on programs the Company supports, and the timing of contract awards by the Department of Defense and subsequently by its prime contractors, which is expected to continue over the next twelve to twenty four months. The Company continues to identify means intended to reduce its variable manufacturing costs to offset the potential impact of low volume of orders to be shipped. However, should order intake fall drastically below the level experienced in the last twenty four months, the Company might be required to implement cost cutting or other downsizing measures to continue its business operations.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the "first-in, first-out" (FIFO) method. The Company buys raw material only to fill customer orders. Excess raw material is created only when a vendor imposes a minimum buy in excess of actual requirements. Such excess material will usually be utilized to meet the requirements of the customer's subsequent orders. If excess material is not utilized after two fiscal years it is fully reserved.

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The Company’s inventory valuation policy is as follows:

Raw material /Work in process:	All material purchased, processed and/or used in the last two fiscal years is valued at the lower of its acquisition cost or market. All material not purchased/used in the last two fiscal years is fully reserved for.
Finished goods:	All finished goods with firm orders for later delivery are valued (material and overhead) at the lower or cost or market. All finished goods with no orders are fully reserved.
Direct labor costs:	Direct labor costs are allocated to finished goods and work in process inventory based on engineering estimates of the amount of man hours required from the different direct labor departments to bring each device to its particular level of completion.

<u>Results of Operations-Three Months Ended August 31, 2008 Compared to Three Months Ended August 31, 2007</u>:

Net sales for the three months ended August 31, 2008 increased 12% to $2,071,000 as compared to $1,847,000 for the three months ended August 31, 2007. This increase was primarily attributable to a higher level of orders that were shipped in accordance with customer requirements.

Cost of sales for the three months ended August 31, 2008 increased to $1,649,000 from $1,551,000 for the comparable period in 2007. Expressed as a percentage of sales, cost of sales decreased to 80% from 84% for the same period in 2007. This change was due primarily to decreases in direct and indirect labor wages and manufacturing overhead expenses.

Gross profit for the three months ended August 31, 2008 increased to $422,000 from $296,000 for the three months ended August 31, 2007. Accordingly, gross margins on the Company’s sales increased to 20% for the three months ended August 31, 2008 in comparison to 16% for the three months ended August 31, 2007. This change was due mainly to higher sales and decreases in direct and indirect labor wages and manufacturing overhead expenses as discussed above.

For the three months ended August 31, 2008, the Company shipped 58,532 units as compared to 205,790 units shipped during the same period of the prior year. It should be noted that since the Company manufactures a wide variety of products with an average sales price ranging from less than one dollar to several hundred dollars, such periodic variations in the Company’s volume of units shipped should not be regarded as a reliable indicator of the Company’s performance.

The Company’s backlog of open orders increased 19%, from $4,886,000 to $5,791,000, for the three months ended August 31, 2008, as compared to an increase of 18% for the three months ended August 31, 2007. Changes in backlog reflect changes in the intake of orders and in the delivery requirements of customers.

The Company has experienced an increase of 9% in the level of bookings during the quarter ended August 31, 2008 as compared to a 61% increase in bookings for the same period in 2007 principally as a result of a shift in defense spending priorities, resulting in an increase in the monetary value of, and timing differences in the placement of contracts by the Department of Defense and its prime contractors.

Selling, general, and administrative expenses decreased to $233,000 for the three months ended August 31, 2008 from $235,000 for the comparable period in 2007. During the three months ended August 31, 2008, selling, general, and administrative expenses as a percentage of net sales fell to 11% as compared with 13% for the three months ended

August 31, 2007. The percentage decrease was due primarily to decreases in sales commissions and selling wages.

Operating income for the three months ended August 31, 2008 increased to $189,000 as compared to $61,000 for the three months ended August 31, 2007. This increase is due mainly to higher sales and decreases in cost of sales and in selling, general and administrative expenses as discussed above.

The Company recorded net other income of $25,000 for the three months ended August 31, 2008 as compared to $43,000 for the three months ended August 31, 2007. Included in net other income was interest income on investment in treasury bills net of changes in market value of $25,000 for the three months ended August 31, 2008 as compared to $46,000 offset by $3,000 of other expense due to the loss of an equipment deposit for the three months ended August 31, 2007. The decrease in interest income is due primarily to lower rates of return on invested funds.

Net income for the three months August 31, 2008 increased to $214,000 as compared to $104,000 for the same period in 2007. This increase is due primarily to higher sales and decreases in cost of sales and selling, general and administrative expenses as discussed above.

Results of Operations-Six Months Ended August 31, 2008 Compared to Six Months Ended August 31, 2007:

Net sales for the six months ended August 31, 2008 increased 18% to $4,240,000 as compared to $3,590,000 for the six months ended August 31, 2007. This increase was primarily attributable to a higher level of orders that were shipped in accordance with customer requirements.

Cost of sales for the six months ended August 31, 2008 increased to $3,272,000 from $2,921,000 for the comparable period in 2007. Expressed as a percentage of sales, cost of sales decreased to 77% from 81% for the same period in 2007. The change was due primarily to decreases in direct and indirect labor wages and manufacturing overhead expenses.

Gross profit for the six months ended August 31, 2008 increased to $968,000 from $669,000 for the six months ended August 31, 2007. Accordingly, gross margins on the Company's sales increased to approximately 23% for the six months ended August 31, 2008 in comparison to approximately 19% for the six months ended August 31, 2007. This change was primarily due to decreases in direct and indirect labor wages and manufacturing overhead expenses as discussed above.

For the six months ended August 31, 2008, the Company shipped 188,109 units as compared to 405,136 units shipped during the same period of the prior year. It should be noted that since the Company manufactures a wide variety of products with an average sales price ranging from less than one dollar to several hundred dollars, such periodic variations in the Company's volume of units shipped should not be regarded as a reliable indicator of the Company's performance.

The Company's backlog of open orders decreased 1%, from $5,826,000 to $5,791,000 for the six months ended August 31, 2008, as compared to an increase of approximately 32% for the six months ended August 31, 2007. Changes in backlog resulted from changes in the intake of orders and in the delivery dates required by customers.

The Company has experienced a decrease in the level of bookings of approximately 16% for the six months ended August 31, 2008 as compared to an increase of 41% for the same period for the previous year principally as a result of a shift in defense spending priorities, resulting in a decrease in the monetary value of, and timing differences in the placement of contracts by the Department of Defense and its prime contractors.

Selling, general, and administrative expenses increased to $517,000 for the six months ended August 31, 2008 from $505,000 for the comparable period in 2007. During the six months ended August 31, 2008, selling, general, and administrative expenses as a percentage of net sales decreased to 12% as compared to 14% for the six months ended August 31, 2007. The increase was due primarily to increases in sales travel and selling wages.

Operating income for the six months ended August 31, 2008 increased to $451,000 from $164,000 for the six months ended August 31, 2007. This increase is due mainly to an increase in sales, and a decrease in cost of sales percentage.

The Company recorded net other income of $35,000 for the six months ended August 31, 2008 as compared to net other income of $91,000 for the six months ended August 31, 2007. Included in net other income was interest income of $35,000 for the six months ended August 31, 2008 as compared to $90,000 for the six months ended August 31, 2007. The decrease in interest income is due primarily to lower interest rates on treasury bills.

Net income for the six months ended August 31, 2008 increased to $486,000 from $255,000 for the same period in 2007. This increase was due primarily to a higher sales volume and lower cost of sales percentage as discussed above.

Liquidity and Capital Resources:

The Company's sole source of cash is revenue generated by ongoing operations. The Company's liquidity might be adversely affected by decreased cash receipts due to anticipated lower level of sales volume over the next twelve to twenty-four months due to customers' delivery requirements. The Company's liquidity is not expected to improve until the Company's revenues increase to a level consistently above its breakeven point.

Furthermore, the Company's liquidity continues to be adversely affected by the Company's 1993 bankruptcy petition obligations and the Company's inability to obtain additional working capital through the sale of debt or equity securities. For a more complete discussion of the Company's bankruptcy obligations, see "Business – Bankruptcy Proceedings" in the Company's Annual Report on Form 10-K filed for the period ended February 29, 2008.

The Company is required to make quarterly payments to holders of unsecured claims until they receive 35 percent (35%) of their pre-petition claims. However, due to negotiations between the parties, the unsecured creditors agreed to a deferment of this payment and the Company agreed to make payments until its obligations are fulfilled. The unsecured creditors do not object to the reduced level of quarterly payments. As of August 31, 2008, the Company has paid approximately $748,000 to its unsecured creditors. The Company's remaining obligation is approximately $1,100,000 to holders of allowed unsecured claims to be paid in quarterly installments.

The Company reported net income of $486,000 and operating income of $451,000 for the six months ended August 31, 2008.

At August 31, 2008, February 29, 2008 and August 31, 2007, the Company had cash of approximately $76,000, $75,000 and $43,000, respectively. Decreases in accounts receivable and inventories contributed $648,000 to the last six months' cash flow generated by ongoing operations.

At August 31, 2008, February 29, 2008 and August 31, 2007, the Company had investments in treasury bills with a market value of approximately $4,979,000, $4,410,000 and $3,837,000, respectively.

At August 31, 2008, the Company had working capital of $6,511,000 as compared with a working capital at August 31, 2007 of $5,454,000. At February 29, 2008, the Company had a working capital of $6,016,000. The $495,000 increase for the six months ended August 31, 2008 was due mainly to a $569,000 increase in investment in treasury bills offset by decreases in accounts receivable and inventories.

Off-Balance Sheet Arrangements:

The Company has not engaged in any off-balance sheet arrangements.

FORWARD-LOOKING STATEMENTS

Some of the statements in this Quarterly Report on Form 10-Q are "forward-looking statements," as that term is defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding our business, financial condition, results of operations, strategies or prospects. You can identify forward-looking statements by the fact that these statements do not relate strictly to historical or current matters. Rather, forward-looking statements relate to anticipated or expected events, activities, trends or results. Because forward-looking statements relate to matters that have not yet occurred, these statements are inherently subject to risks and uncertainties. Many factors could cause our actual activities or results to differ materially from the activities and results anticipated in forward-looking statements. These factors include those described under the caption "Risk Factors" in our Annual Report on Form 10-K for the year ended February 29, 2008, including those identified below. We do not undertake any obligation to update forward-looking statements.

Some of the factors that may impact our business, financial condition, results of operations, strategies or prospects include:

- Our complex manufacturing processes may lower yields and reduce our revenues.

- Our business could be materially and adversely affected if we are unable to obtain qualified supplies of raw materials and parts on a timely basis and at a cost-effective price.
- We are dependent on government contracts, which are subject to termination, price renegotiations and regulatory compliance, which can increase the cost of doing business and negatively impact our revenues.
- Changes in government policy or economic conditions could negatively impact our results.
- Our inventories may become obsolete and other assets may be subject to risks.
- Environmental regulations could require us to incur significant costs.
- Our business is highly competitive, and increased competition could reduce gross profit margins and the value of an investment in our Company.
- Downturns in the business cycle could reduce the revenues and profitability of our business.
- Our operating results may decrease due to the decline of profitability in the semiconductor industry.
- Uncertainty of current economic conditions, domestically and globally, could continue to affect demand for our products and negatively impact our business.
- Cost reduction efforts may be unsuccessful or insufficient to improve our profitability and may adversely impact productivity.
- Our inability to introduce new products could result in decreased revenues and loss of market share to competitors; new technologies could also reduce the demand for our products.
- Loss of, or reduction of business from, substantial clients could hurt our business by reducing our revenues, profitability and cash flow.
- A shortage of three-inch silicon wafers could result in lost revenues due to an inability to build our products.
- The nature of our products exposes us to potentially significant product liability risk.
- We depend on the recruitment and retention of qualified personnel, and our failure to attract and retain such personnel could seriously harm our business.
- Provisions in our charter documents and rights agreement could make it more difficult to acquire our Company and may reduce the market price of our stock.
- Natural disasters, like hurricanes, or occurrences of other natural disasters whether in the United States or internationally may affect the markets in which our common stock trades, the markets in which we operate and our profitability.
- Natural disasters, like hurricanes, or occurrences of other natural disasters whether in the United States or internationally may affect the availability of raw materials which may adversely affect our profitability.
- Failure to protect our proprietary technologies or maintain the right to use certain technologies may negatively affect our ability to compete.
- The price of our common stock has fluctuated widely in the past and may fluctuate widely in the future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Not applicable

ITEM 4. CONTROLS AND PROCEDURES

Our Evaluation of Disclosure Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of its management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report.

Changes in Internal Control over Financial Reporting

Based on an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, there has been no change in our internal control over financial reporting during our last fiscal quarter identified in connection with that evaluation, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II– OTHER INFORMATION

ITEM 6. EXHIBITS:

Exhibits

31 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

SOLITRON DEVICES, INC.

Date: October 15, 2008

/s/ Shevach Saraf
Shevach Saraf
Chairman, President,
Chief Executive Officer,
Treasurer and
Chief Financial Officer

EXHIBIT INDEX

EXHIBIT NUMBER	DESCRIPTION
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