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AMERICAN AMMUNITION INC/FL
Form 10QSB
May 23, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

Form 10-QSB

(Mark one)

Quarterly Report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2005

Transition Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission File No.: 000-32379

American Ammunition, Inc.

(Name of small business registrant in its charter)

California

(State or other jurisdiction of incorporation or organization)

3545 NW 71st Street
Miami, FL

(Address of principal executive offices)

91-2021594

(I.R.S. Employer Identification No.)

33147

(Zip Code)

Registrant's telephone number: (305) 835-7400

Securities registered under Section 12(b) of the Exchange Act:

Title of each class

Name of each exchange on which registered

None

Securities registered under Section 12(g) of the Exchange Act:

Common Stock, \$0.001 par value

(Title of class)

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Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date: May 21, 2005: 74,851,691

Transitional Small Business Disclosure Format (check one): YES NO

American Ammunition, Inc.

Form 10-QSB for the Quarter ended March 31, 2005

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Part I - Financial Information

Item 1 - Financial Statements

American Ammunition, Inc. and Subsidiaries
Consolidated Balance Sheets
March 31, 2005 and 2004

(Unaudited)

| | March 31, 2005 | |
|--|--------------------------|-------|
| | ----- | ----- |
| ASSETS | | |
| Current Assets | | |
| Cash on hand and in bank | \$ 377,922 | \$ |
| Accounts receivable - trade, net of allowance for doubtful accounts of \$-0- and \$-0-, respectively | 289,559 | |
| Inventory | 857,552 | |
| Prepaid expenses | 59,497 | |
| | ----- | ----- |
| Total Current Assets | 1,584,530 | |
| | ----- | ----- |
| Property and Equipment - at cost | | |
| Manufacturing equipment | 8,006,483 | |
| Office furniture and fixtures | 69,889 | |
| Leasehold improvements | 190,277 | |
| | ----- | ----- |
| Accumulated depreciation | 8,266,649 (4,990,261) | (|
| | ----- | ----- |
| Net Property and Equipment | 3,276,388 | |
| | ----- | ----- |
| Other Assets | | |
| Patents, Trademarks and Noncompetition agreement, net of accumulated amortization of approximately \$22,974 | 252,716 | |
| Deposits and other | 83,660 | |
| | ----- | ----- |
| Total other assets | 336,376 | |
| | ----- | ----- |
| TOTAL ASSETS | \$ 5,197,294 | \$ |
| | ===== | ===== |

- Continued -

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The financial information presented herein has been prepared by management without audit by independent certified public accountants.

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

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American Ammunition, Inc. and Subsidiaries Consolidated Balance Sheets - Continued March 31, 2005 and 2004

(Unaudited)

| | March 31, 2005 | |
|---|------------------------|-------|
| | ----- | ----- |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current Liabilities | | |
| Current maturities of leases payable | \$ - | \$ |
| Customer deposits | 440,906 | |
| Accounts payable - trade | 693,980 | |
| Accrued salaries and wages payable | 166,492 | |
| Accrued interest expense | 15,000 | |
| Accrued dividends payable | 29,509 | |
| | ----- | ----- |
| Total Current Liabilities | 1,345,887 | |
| Long-Term Liabilities | | |
| | - | |
| | ----- | ----- |
| Total Liabilities | 1,345,887 | |
| | ----- | ----- |
| Commitments and Contingencies | | |
| Convertible Debenture | | |
| | 266,365 | |
| | ----- | ----- |
| Stockholders' Equity | | |
| Preferred stock - \$0.001 par value 20,000,000 shares authorized. 1,795,320 shares allocated to Series A 91,700 shares allocated to Series B 1,905,882 shares allocated to Series C | 2,010 | |
| Common stock - \$0.001 par value. 300,000,000 shares authorized. 74,851,691 and 69,331,666 shares issued and outstanding, respectively | 74,852 | |
| Additional paid-in capital | 24,472,709 | 2 |
| Accumulated deficit | (20,789,529) | (1 |
| | ----- | ----- |
| Stock subscription receivable | 3,760,042 (175,000) | |
| | ----- | ----- |
| Total Stockholders' Equity | 3,585,042 | |
| | ----- | ----- |

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TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY \$ 5,197,294 \$
===== =====

The financial information presented herein has been prepared by management without audit by independent certified public accountants.

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

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American Ammunition, Inc. and Subsidiaries Consolidated Statements of Operations and Comprehensive Loss Three months ended March 31, 2005 and 2004

(Unaudited)

| | Three months ended March 31, 2005 | T M |
|--|---|--------|
| | ----- | ----- |
| Revenues - net of returns and allowances | \$ 1,170,317 | \$ |
| | ----- | ----- |
| Cost of Sales | | |
| Materials, Direct Labor and other direct costs | 1,349,331 | |
| Depreciation | 187,249 | |
| | ----- | ----- |
| Total Cost of Sales | 1,536,580 | |
| | ----- | ----- |
| Gross Profit | (366,263) | |
| | ----- | ----- |
| Operating Expenses | | |
| Research and development expenses | 1,732 | |
| Marketing and selling expenses | 81,106 | |
| Other operating expenses | 319,561 | |
| Bad debt expense | - | |
| Interest expense | 6,520 | |
| Depreciation expense | 1,317 | |
| Amortization expense | 13,785 | |
| Compensation expense related to issuances of common stock at less than "fair value" | - | |
| | ----- | ----- |
| Total Operating Expenses | 424,021 | |
| | ----- | ----- |
| Loss from Operations | (790,284) | |
| | ----- | ----- |
| Other Income (Expense) | 4,240 | |
| | ----- | ----- |
| Loss before Income Taxes | (786,044) | |
| | ----- | ----- |
| Provision for Income Taxes | - | |
| | ----- | ----- |
| Net Loss | (786,044) | |

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| | |
|---|-----------------|
| Other Comprehensive Income | - |
| | ----- |
| Comprehensive Loss | \$ (786,044) \$ |
| | ===== |
| Loss per weighted-average share of common stock outstanding, computed on net loss - basic and fully diluted | \$ (0.01) \$ |
| | ===== |
| Weighted-average number of common shares outstanding | 74,851,691 |
| | ===== |

The financial information presented herein has been prepared by management without audit by independent certified public accountants.

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

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American Ammunition, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Three months ended March 31, 2005 and 2004

(Unaudited)

| | Three months ended March 31, 2005 |
|---|---|
| | ----- |
| Cash flows from operating activities | |
| Net loss for the period | \$ (786,045) \$ |
| Adjustments to reconcile net loss to net cash provided by operating activities | |
| Depreciation and amortization | 202,351 |
| Bad debt expense | - |
| Compensation expense related to issuance of common stock at less than "fair value" | - |
| (Increase) Decrease in | |
| Accounts receivable | 349,885 |
| Inventory | 54,872 |
| Prepaid expenses, deposits and other | (651) |
| Increase (Decrease) in | |
| Accounts payable - trade | (242,906) |
| Other accrued expenses | 30,522 |
| | ----- |
| Net cash (used in) operating activities | (391,972) |
| | ----- |
| Cash flows from investing activities | |
| Purchase of property and equipment | (35,571) |

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| | |
|--|------------|
| Net cash (used in) investing activities | (35,571) |
| Cash flows from financing activities | |
| Principal paid on long-term capital leases | - |
| Cash received from sale of common stock and warrant exercise | - |
| Net cash provided by financing activities | - |
| Increase (Decrease) in Cash | (427,543) |
| Cash at beginning of period | 805,465 |
| Cash at end of period | \$ 377,922 |
| Supplemental disclosure of interest and income taxes paid | |
| Interest paid for the period | \$ 6,520 |
| Income taxes paid for the period | \$ - |
| Supplemental disclosure of non-cash investing and financing activities | |
| Conversion of convertible debenture into common stock | \$ - |

The financial information presented herein has been prepared by management without audit by independent certified public accountants.

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

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American Ammunition, Inc. and Subsidiaries
Notes to Consolidated Financial Statements

Note A - Organization and Description of Business

American Ammunition, Inc. (AAI or Company) was incorporated on February 1, 2000 in accordance with the Laws of the State of California. The Company functions as a holding company providing management oversight services to it's wholly-owned operating subsidiaries; F&F Equipment, Inc. and Industrial Plating Enterprise Co.

F&F Equipment, Inc.(F&F) was incorporated on October 4, 1983 in accordance with the Laws of the State of Florida. F&F is engaged in the design, manufacture and international sales of small arms ammunition. F&F has conducted its business operations under the assumed name of "American Ammunition" since its inception.

Industrial Plating Enterprise Co. (IPE), which was incorporated and commenced production on June 14, 2002. IPE is a fully licensed and approved state of the art electrochemical metallization facility for processing the Company's line of small arms projectiles as well as other products and services while employing

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environmentally sound water conservation and proven waste treatment techniques. The facility meets or exceeds all current environmental requirements and enjoys the "conditionally exempt small quantity generator" status for State and Federal regulations. All activities of IPE since its inception have been dedicated to the needs and demands of F&F.

Note B - Preparation of Financial Statements

The Company and its subsidiaries follow the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America and have adopted a year-end of December 31 for all entities.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented

For segment reporting purposes, the Company operated in only one industry segment during the periods represented in the accompanying financial statements and makes all operating decisions and allocates resources based on the best benefit to the Company as a whole.

The accompanying consolidated financial statements contain the accounts of American Ammunition, Inc. and its wholly-owned subsidiaries, F&F Equipment, Inc. and Industrial Plating Enterprise Co. All significant intercompany transactions have been eliminated. The consolidated entities are collectively referred to as "Company".

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American Ammunition Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note C - Summary of Significant Accounting Policies

1. Cash and cash equivalents

For Statement of Cash Flows purposes, the Company considers all cash on hand and in banks, certificates of deposit and other highly-liquid investments with maturities of three months or less, when purchased, to be cash and cash equivalents.

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Cash overdraft positions may occur from time to time due to the timing of making bank deposits and releasing checks, in accordance with the Company's cash management policies.

2. Accounts receivable and Revenue Recognition

In the normal course of business, the Company extends unsecured credit to virtually all of its customers which are located throughout the United States. Because of the credit risk involved, management has provided an allowance for doubtful accounts which reflects its opinion of amounts which will eventually become uncollectible. In the event of complete non-performance, the maximum exposure to the Company is the recorded amount of trade accounts receivable shown on the balance sheet at the date of non-performance.

The Company ships all product on an FOB-Plant, "as-is" basis. Accordingly, revenue is recognized by the Company at the point at which an order is shipped at a fixed price, collection is reasonably assured and the Company has no remaining performance obligations related to the sale. The Company sells all products with "no right of return" by the purchaser for any factor other than defects in the product's production.

On rare occasion, the Company may elect to accept product returns from customers on a case-by-case basis to offset unpaid accounts receivable. These situations are a "last case" scenario and are initiated by senior management through negotiations with the respective customer.

3. Inventory

Inventory consists of raw materials, work-in-process and finished goods related to the production and sale of small arms ammunition. Inventory is valued at the lower of cost or market using the first-in, first-out method.

4. Property, plant and equipment

Property and equipment are recorded at historical cost. These costs are depreciated over the estimated useful lives of the individual assets using the straight-line method, generally three to ten years.

Gains and losses from disposition of property and equipment are recognized as incurred and are included in operations.

5. Income Taxes

The Company uses the asset and liability method of accounting for income taxes. At March 31, 2005 and 2004, the deferred tax asset and deferred tax liability accounts, as recorded when material to the financial statements, are entirely the result of temporary differences. Temporary differences represent differences in the recognition of assets and liabilities for tax and financial reporting purposes, primarily accumulated depreciation and amortization, allowance for doubtful accounts and vacation accruals.

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American Ammunition Inc. and Subsidiaries

Notes to Consolidated Financial Statements - Continued

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Note C - Summary of Significant Accounting Policies - Continued

5. Income Taxes - continued

As of March 31, 2005 and 2004, the deferred tax asset related to the Company's net operating loss carryforward is fully reserved. If these carryforwards are not utilized, they will begin to expire at the end of 2005.

6. Earnings (loss) per share

Basic earnings (loss) per share is computed by dividing the net income (loss) available to common shareholders by the weighted-average number of common shares outstanding during the respective period presented in our accompanying financial statements.

Fully diluted earnings (loss) per share is computed similar to basic income (loss) per share except that the denominator is increased to include the number of common stock equivalents (primarily outstanding options and warrants).

Common stock equivalents represent the dilutive effect of the assumed exercise of the outstanding stock options and warrants, using the treasury stock method, at either the beginning of the respective period presented or the date of issuance, whichever is later, and only if the common stock equivalents are considered dilutive based upon the Company's net income (loss) position at the calculation date.

As of March 31, 2005 and 2004, and subsequent thereto, the Company had no options outstanding. The outstanding warrants and convertible preferred stock and mandatorily convertible debentures are anti-dilutive due to the Company's net operating loss position.

7. Advertising costs

The Company does not conduct any direct response advertising activities. For non-direct response advertising, the Company charges the costs of these efforts to operations at the first time the related advertising is published.

Note D - Fair Value of Financial Instruments

The carrying amount of cash, accounts receivable, accounts payable and notes payable, as applicable, approximates fair value due to the short term nature of these items and/or the current interest rates payable in relation to current market conditions.

Interest rate risk is the risk that the Company's earnings are subject to fluctuations in interest rates on either investments or on debt and is fully dependent upon the volatility of these rates. The Company does not use derivative instruments to moderate its exposure to interest rate risk, if any.

Financial risk is the risk that the Company's earnings are subject to fluctuations in interest rates or foreign exchange rates and are fully dependent upon the volatility of these rates. The company does not use derivative instruments to moderate its exposure to financial risk, if any.

Note E - Concentrations of Credit Risk

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The Company maintains its cash accounts in a single financial institutions subject to insurance coverage issued by the Federal Deposit Insurance Corporation (FDIC). Under FDIC rules, the Company and its subsidiaries are entitled to aggregate coverage of \$100,000 per account type per separate legal entity per financial institution.

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American Ammunition Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note E - Concentrations of Credit Risk - Continued

During the period ended March 31, 2005 and the periods subsequent thereto, respectively, the various operating companies maintained deposits in this financial institution with credit risk exposures in excess of statutory FDIC coverage. The Company incurred no losses during 2003 and 2004, and subsequent thereto, as a result of any of these unsecured situations.

Note F - Inventory

As of March 31, 2005 and 2004, inventory consisted of the following components:

| | March 31, 2005 | March 31, 2004 | |
|-----------------|-------------------|-------------------|--|
| | ----- | ----- | |
| Raw materials | \$ 596,548 | \$ 428,611 | |
| Work in process | 177,862 | 419,236 | |
| Finished goods | 83,142 | 497,739 | |
| | ----- | ----- | |
| Totals | \$ 857,552 | \$1,345,586 | |
| | ===== | ===== | |

Note G - Property and Equipment

Property and equipment consist of the following components:

| | March 31, 2005 | March 31, 2004 | Estimated useful life |
|-------------------------------|--------------------------|--------------------------|--------------------------|
| | ----- | ----- | |
| Manufacturing equipment | \$ 8,006,483 | \$ 7,416,352 | 3-10 years |
| Office furniture and fixtures | 69,889 | 77,381 | 3- 7 years |
| Leasehold improvements | 190,277 | 187,397 | 8-20 years |
| | ----- | ----- | |
| Accumulated depreciation | 8,266,649 (4,990,261) | 7,681,130 (4,241,372) | |
| | ----- | ----- | |
| Net property and equipment | \$ 3,276,388 | \$ 3,439,758 | |
| | ===== | ===== | |

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Total depreciation expense charged to operations for the three months ended March 31, 2005 and 2004 was approximately \$188,566 and \$171,982, respectively.

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American Ammunition, Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note H- Capital Leases Payable

Capital leases payable consist of the following as of March 31, 2005 and 2004, respectively:

| | March 31, 2004 | March 31, 2003 |
|--|-------------------|-------------------|
| | ----- | ----- |
| Three capital leases, respectively, payable to various equipment financing companies. Interest, at March 31, 2002, ranging between 11.37% and 14.05%. Payable in aggregate monthly installments of approximately \$935, including accrued interest. Final maturities occur between September 2004 and December 2004. Collateralized the underlying leased manufacturing equipment. | \$ - | \$ 4,905 |
| Less current maturities | - | (4,905) |
| | ----- | ----- |
| Long-term portion | \$ - | \$ - |
| | ===== | ===== |

Note I - Convertible Debenture

The Company entered into a Securities Purchase Agreement with La Jolla Cove Investors, Inc. ("La Jolla") on October 4, 2002 for the sale of (i) \$250,000 in convertible debentures and (ii) warrants to buy 30,000,000 shares of our common stock. On March 13, 2003 and May 6, 2003, La Jolla advanced an aggregate of \$350,000 to our company which such funding was allocated towards the principal balance of our convertible debentures.

As of March 31, 2005, the outstanding balance on the convertible debenture is approximately \$266,365 and we have approximately 2,663,650 warrants outstanding. A recap of the debenture activity is as follows:

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| | Debenture (in dollars) | Warrant (in shares) |
|---|---------------------------|------------------------|
| | ----- | ----- |
| Initial amount | \$ 600,000 | 6,000,000 |
| 2003 redemptions | (208,635) | (2,086,350) |
| 2004 redemptions | (125,000) | (1,250,000) |
| | ----- | ----- |
| Balances outstanding at March 31, 2005 | \$ 266,365 ===== | 2,633,650 ===== |

The debentures bear interest at 8%, mature on June 30, 2006, and are convertible into our common stock, at the selling stockholder's option. The convertible debentures are convertible into the number of our shares of common stock equal to the principal amount of the debentures being converted multiplied by 11, less the product of the conversion price multiplied by 10 times the dollar amount of the debenture. The conversion price for the convertible debentures is the lesser of (i) \$1.00 or (ii) seventy six percent of the average of the five lowest volume weighted average prices during the twenty (20) trading days prior to the conversion. Accordingly, there is in fact no limit on the number of shares into which the debenture may be converted. However, in the event that our market price is less than \$.30, we will have the option to prepay the debenture at 125% rather than have the debenture converted. In addition, the selling stockholder is obligated to exercise the warrant concurrently with the submission of a conversion notice by the selling stockholder. As of March 31, 2005, the warrant is exercisable into 2,663,650 shares of common stock at an exercise price of \$1.00 per share.

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American Ammunition, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - Continued

Note I - Convertible Debenture - Continued

In December 2004, the Company entered into an addendum to the convertible debenture and warrant whereby the Company agreed to the following:

- * the discount multiplier was reduced from eighty percent to seventy six percent;
- * within five business days after this registration statement being declared effective, La Jolla is required to submit a debenture conversion in the amount of \$10,000 and every ten business days thereafter La Jolla shall submit three additional debenture conversion in the amount of \$10,000 each;
- * within five business days after this registration statement being declared effective, La Jolla shall wire \$400,000 to us as a prepayment towards the exercise of its warrant; and
- * immediately following the sale of all shares held by La Jolla in connection with the debenture conversions in the aggregate amount of \$40,000, La Jolla shall wire \$275,000 to us as a prepayment towards the exercise of its warrant and shall submit a debenture conversion in the amount of \$6,250 on the first business day of each month until the debenture is no longer outstanding.

LaJolla has contractually agreed to restrict its ability to convert or exercise

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its warrants and receive shares of our common stock such that the number of shares of common stock held by them and their affiliates after such conversion or exercise does exceed 4.9% of the then issued and outstanding shares of common stock.

Due to the contractually agreed mandatory conversion of this Debenture, the Company has reflected this transaction in its balance sheet as a "mezzanine" level debt obligation on its balance sheet, between "Total Liabilities" and "Stockholders' Equity". Upon the respective mandatory conversion, the Company will relieve the respective portion of the Debenture and the any related accrued, but unpaid interest, and credit this amount to the respective "common stock" and "additional paid-in capital" accounts in the stockholder's equity section for the par value and excess amount over the par value of the respective shares issued.

As the warrant is non-detachable from the Debenture and requires simultaneous exercise upon conversion of the Debenture, no value was assigned to the issued warrant. Upon exercise of the warrant, the Company will record the issuance of the underlying shares as a new issuance of common stock on the date of each respective exercise.

On various dates through December 31, 2003, the Debenture Holder elected to convert an aggregate \$208,635, through 24 separate transactions, in outstanding Debenture principal into restricted, unregistered common stock. This election caused the Company to issue 4,561,753 shares of restricted, unregistered common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 2,086,350 shares of the Company's restricted, unregistered common stock for gross proceeds of \$2,086,350.

On various dates between January 1, 2004 and December 31, 2004, the Debenture Holder elected to convert an aggregate \$125,000, through 6 separate transactions, in outstanding Debenture principal into registered common stock. This election caused the Company to issue 4,150,000 shares of common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 1,250,000 shares of the Company's common stock for gross proceeds of \$1,250,000. As of December 31, 2004, an aggregate of 1,000,000 shares of the Company's common stock have been issued by the Company and are being held in escrow by the Company's counsel pending receipt of the final \$150,000 from the Debenture Holder.

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American Ammunition, Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note J - Preferred Stock Transactions

Preferred stock consists of the following as of March 31, 2005 and 2004, respectively:

| March 31, 2005 | | March 31, 2004 | |
|----------------|-------|----------------|-------|
| ----- | | ----- | |
| # shares | value | # shares | value |

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| | | | | |
|-----------------------------|-----------|------------|---------|------------|
| | ----- | ----- | ----- | ----- |
| Series A Cumulative | | | | |
| Convertible Preferred Stock | 12,000 | \$ 60,000 | 12,000 | \$ 60,000 |
| Series B Cumulative | | | | |
| Convertible Preferred Stock | 91,700 | 458,500 | 91,700 | 458,500 |
| Series C Convertible | | | | |
| Preferred Stock | 1,905,882 | 324,000 | - | - |
| | ----- | ----- | ----- | ----- |
| | 2,009,582 | \$ 842,500 | 103,700 | \$ 518,500 |
| | ===== | ===== | ===== | ===== |

Series A Convertible Preferred Stock

In September, October and November 2001, the Company sold an aggregate 222,600 shares of \$5.00 Series A Convertible Preferred Stock (Series A Preferred Stock) for total proceeds of approximately \$1,113,000 through a Private Placement Memorandum. The Series A Convertible Preferred Stock provides for cumulative dividends at a rate of 8.0% per year, payable quarterly, in cash or shares of the Company's common stock at the Company's election. Each share of Series A Preferred Stock is convertible into 11 shares of the Company's common stock initially at any time after 6 months of the date of issue and prior to the notice of redemption at the option of the holder, subject to adjustments for customary anti-dilution events. In December 2001, at the request of the holders of the Series A Preferred Stock, the Company and the individual holders modified the holding period for conversion to allow for conversion in December 2001.

In September 2001, the Company's principal stockholder converted approximately \$4,007,327 of unsecured debt and approximately \$3,546,273 of cumulative and unpaid accrued interest into 1,510,710 shares of Series A Preferred Stock.

In September 2001, a creditor of the Company agreed to convert approximately \$10,000 of trade accounts payable into 2,000 shares of Series A Preferred Stock.

In December 2001, concurrent with a modification in the holding period prior to conversion, certain holders of the Series A Preferred Stock orally notified the Company of their intent to exercise the conversion features on 1,749,720 issued and outstanding shares of Series A Preferred Stock into 19,246,920 shares of common stock prior to December 31, 2001. Due to the timing of the requisite documentation, the clerical activities related to this conversion were not completed until February 2002.

In conjunction with the Series A Preferred Stock, certain shares were sold after the Company's common stock was approved for trading by the National Association of Securities Dealers on the OTC Bulletin Board in October 2001. The shares of Series A Preferred Stock sold subsequent to this date had an equivalent per share value of common stock below the ending quoted market price of the Company's common stock on their respective issue dates. This difference created a Beneficial Conversion Feature Discount of approximately \$1,207,993. This discount was then amortized over the unexpired time period between the date of issue of the eligible shares and the eligible conversion date, as amended. All of the shares sold subsequent to the initial trading date were converted in December 2001 and, accordingly, the approximate \$1,207,993 in Beneficial Conversion Feature Discount was fully amortized to operations.

In December 2002, a holder of 5,000 shares of Series A Preferred Stock exercised his conversion rights and converted these shares of Series A Preferred Stock into 55,000 shares of restricted, unregistered common stock.

In January 2003, three separate holders of 9,000 shares of Series A Preferred Stock exercised their conversion rights and converted these shares of Series A Preferred stock into 99,000 shares of restricted, unregistered common stock.

American Ammunition, Inc. and Subsidiaries
Notes to Consolidated Financial Statements - Continued

Note J - Preferred Stock Transactions - Continued

Series B Convertible Preferred Stock

In May 2003, the Company sold an aggregate 91,700 shares of \$5.00 Series B Convertible Preferred Stock (Series B Preferred Stock) for total proceeds of approximately \$458,500 through a separate Private Placement Memorandum. The Series B Convertible Preferred Stock provides for cumulative dividends at a rate of 8.0% per year, payable quarterly, in cash or shares of the Company's common stock at the Company's election. Each share of Series B Preferred Stock is convertible into 11 shares of the Company's common stock initially at any time after 6 months of the date of issue and prior to the notice of redemption at the option of the holder, subject to adjustments for customary anti-dilution events.

Series C Convertible Preferred Stock

In November 2004, the Company sold 1,905,882 shares of Series C Convertible Preferred Stock to an existing shareholder and officer of the Company in a private transaction pursuant to Section (4)2 of the Securities Act of 1933 for gross proceeds of approximately \$324,000. No underwriter was used in conjunction with this transaction.

The Series C Convertible Preferred Stock provides for dividends at a rate of 4.0% per annum, to be declared and paid monthly in either cash or stock at the discretion of the Company.

Each share of Series C Preferred Stock is convertible at a rate of \$0.18 per share into 1,800,000 shares of the Company's common stock at any time at the option of the holder, subject to adjustments for customary anti-dilution events.

Note K - Common Stock Transactions

Calendar 2003 transactions

During the period from March 19, 2003 through December 31, 2003, the Company issued an aggregate 4,561,753 shares of common stock, in 24 separate transactions, in exchange for the redemption of approximately \$208,635 in outstanding debenture balance and approximately \$2,086,350 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to operations of approximately \$882,291 during this time period.

In January 2003, the Company issued an aggregate 937,568 shares of restricted, unregistered common stock for cash proceeds of approximately \$324,182. These

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sales were made at a price of either \$0.23 or \$0.36 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used for operating working capital.

In February 2003, the Company issued 384,615 shares of restricted, unregistered common stock for cash proceeds of approximately \$100,000. These sales were made at a price of \$0.26 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used to reduce the Company's outstanding long-term debt.

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American Ammunition, Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note K - Common Stock Transactions - Continued

Calendar 2003 transactions - continued

In March 2003, the Company issued 972,222 shares of restricted, unregistered common stock for cash proceeds of approximately \$350,000. These sales were made at a price of \$0.36 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used to reduce the Company's outstanding long-term debt.

In May 2003, the Company issued 1,967 shares of restricted, unregistered common stock in payment of approximately \$1,200 in accrued dividends payable on the Company's outstanding Series A Preferred Stock for the quarter ended March 31, 2003.

In October 2003, in a separate transaction, the Company sold 2,200,000 shares of restricted, unregistered common stock to the Debenture Holder for cash proceeds of approximately \$400,000, or approximately \$0.18 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The cash proceeds of this transaction were used to provide working capital and support operations.

In October 2003, the Company issued an aggregate 37,866 shares of restricted, unregistered common stock in payment of approximately \$16,710 in accrued dividends payable on the Company's outstanding Series A and Series B Preferred Stock for the quarters ended June 30, 2003 and September 30, 2003, collectively.

Calendar 2004 transactions

During the period from February 13, 2004 through June 4, 2004, the Company issued an aggregate 4,150,000 shares of common stock, in 5 separate transactions, in exchange for the redemption of approximately \$125,000 in outstanding debenture balance and approximately \$1,250,000 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's

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common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to operations of approximately \$356,000 during this time period.

Additionally, on June 29, 2004, the Company issued an additional 1,000,000 shares of common stock in advance of the exercise of a \$25,000 redemption on the outstanding debenture payable and a \$250,000 cash payment on the exercise of the affiliated warrant. As of December 31, 2004, the Company has received \$100,000 in cash on the warrant exercise and has not applied the debt reduction portion of this transaction.

In January 2004, the Company issued 38,038 shares of restricted, unregistered common stock in payment of approximately \$10,000 in accrued dividends payable on the Company's outstanding Series A and Series B Preferred Stock for the quarter ended December 31, 2003. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

In May 2004, the Company issued 25,260 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended March 31, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

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American Ammunition, Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note K - Common Stock Transactions - Continued

Calendar 2004 transactions - Continued

On May 26, 2004, the Company issued 300,000 shares of restricted, unregistered common stock to two separate corporations in payment and full satisfaction of all amounts due for fees and/or commissions due in conjunction with the Company's convertible debenture financing transaction. This transaction was valued at approximately \$36,000, which was less than the closing price on the date of the respective transaction resulted in a charge to operations of approximately \$24,000. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

In August 2004, the Company issued 29,746 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended June 30, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

On October 19, 2004, the Company issued 1,111,112 shares of restricted,

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unregistered common stock to acquire certain assets valued at an aggregate \$500,000. The assets consist principally of equipment (approximately \$134,000), inventory (approximately \$89,500) and patents and a covenant not-to-compete (approximately \$276,500).

In November 2004, the Company issued 53,908 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended June 30, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

Note L - Rental Commitments

The Company leases its corporate office and manufacturing facility from its controlling stockholder under a long-term operating lease agreement. The lease requires a monthly payment of approximately \$5,735, including applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. The lease expires on December 1, 2009 and contains a clause that upon expiration, the Company and the controlling shareholder shall renegotiate the annual rental amount.

The Company's subsidiary, IPE, leases its manufacturing facility from an unrelated third-party under a long-term operating lease agreement. This lease is for a period of five (5) years and requires graduated monthly payments, changing on the lease anniversary date, ranging from approximately \$1,751 to \$1,914, plus the applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. The lease expires on February 28, 2007 and may be renewed for an additional five (5) year term at a rental rate of approximately \$1,971, plus applicable sales taxes for the first renewal year and 3.0% increase on each succeeding anniversary date. Total rent expense under this lease was approximately \$20,752 and \$16,622, respectively, for each of the years ended December 31, 2004 and 2003.

In May 2004, the Company entered into a long-term lease agreement for a warehouse facility adjacent to the Company's primary office and manufacturing facility. This lease is for a period of two (2) years and requires payments of approximately \$6,206 per month for the first 12 months and approximately \$6,393 for the second 12 months, plus applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. This lease expires on May 31, 2006. Further, the Company is responsible for any incremental real estate taxes and property insurance in excess of the amounts incurred by the landlord for the calendar year immediately preceding the execution of the lease.

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American Ammunition, Inc. and Subsidiaries Notes to Consolidated Financial Statements - Continued

Note L - Rental Commitments - Continued

Future minimum rental payments on the above leases are as follows:

| Year ended | |
|--------------|--------|
| December 31, | Amount |

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| | |
|--------|------------|
| 2005 | \$ 166,974 |
| 2006 | 117,244 |
| 2007 | 72,643 |
| 2008 | 68,815 |
| 2007 | 68,815 |
| Totals | \$ 494,491 |

For the respective years ended December 31, 2004, the Company paid an aggregate of \$131,804 and \$87,826 for rent under these agreements.

Note M - Income Taxes

The components of income tax (benefit) expense for the respective three month periods ended March 31, 2005 and 2004 are as follows:

| | Three months ended March 31, 2005 | Three months ended March 31, 2004 |
|----------|---|---|
| Federal: | | |
| Current | \$ - | \$ - |
| Deferred | - | - |
| | ----- | ----- |
| | - | - |
| | ----- | ----- |
| State: | | |
| Current | - | - |
| Deferred | - | - |
| | ----- | ----- |
| | - | - |
| | ----- | ----- |
| Total | \$ - | \$ - |
| | ===== | ===== |

As of December 31, 2004, the Company has a net operating loss carryforward of approximately \$8,100,000 to offset future taxable income. Subject to current regulations, components of this carryforward began to expire at the end of Calendar 2003. The amount and availability of the net operating loss carryforwards may be subject to limitations set forth by the Internal Revenue Code. Factors such as the number of shares ultimately issued within a three year look-back period; whether there is a deemed more than 50 percent change in control; the applicable long-term tax exempt bond rate; continuity of historical business; and subsequent income of the Company all enter into the annual computation of allowable annual utilization of the carryforwards.

The Company's income tax expense (benefit) for the three months ended March 31, 2005 and 2004, respectively, differed from the statutory federal rate of 34 percent as follows:

| | Three months ended March 31, 2005 | Three months ended March 31, 2004 |
|--|---|---|
| Statutory rate applied to loss before income taxes | \$ (267,000) | \$ (295,000) |
| Increase (decrease) in income taxes resulting from: | | |

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| | | |
|--|---------|---------|
| State income taxes | - | - |
| Other, including reserve for deferred tax asset | 267,000 | 295,000 |
| | ----- | ----- |
| Income tax expense | \$ - | \$ - |
| | ===== | ===== |

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American Ammunition, Inc. and Subsidiaries

Notes to Consolidated Financial Statements - Continued

Note O - Income Taxes - Continued

Temporary differences, consisting primarily of the net operating loss carryforward and statutory differences in the depreciable lives for property and equipment, between the financial statement carrying amounts and tax bases of assets and liabilities give rise to deferred tax assets and liabilities as of December 31, 2004 and 2003, respectively:

| | December 31, 2004 | December 31, 2003 |
|--------------------------------------|----------------------|----------------------|
| | ----- | ----- |
| Deferred tax assets - long-term | | |
| Net operating loss carryforwards | \$ 2,669,000 | \$ 2,900,000 |
| Deferred tax liabilities - long-term | | |
| Statutory depreciation differences | (690,000) | (250,000) |
| | ----- | ----- |
| | 1,979,000 | 2,650,000 |
| Less valuation allowance | (1,979,000) | (2,650,000) |
| | ----- | ----- |
| Net Deferred Tax Asset | \$ - | \$ - |
| | ===== | ===== |

During the years ended December 31, 2004 and 2003, respectively, the valuation allowance increased (decreased) by approximately \$(671,000) and \$656,000.

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Item 2 - Management's Discussion and Analysis or Plan of Operation

Caution Regarding Forward-Looking Information

Certain statements contained in this Registration Statement including, without limitation, statements containing the words "believes", "anticipates", "expects" and words of similar import, constitute forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

Such factors include, among others, the following: international, national and local general economic and market conditions; demographic changes; the ability of the Company to sustain, manage or forecast its growth; the ability of the Company to successfully make and integrate acquisitions; raw material costs and availability; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers or suppliers; fluctuations and difficulty in forecasting operating results; changes in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; and other factors referenced in this and previous filings.

Given these uncertainties, readers of this Quarterly Report on Form 10-QSB and investors in our equity securities are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

General

American Ammunition, Inc. is a holding company with two operating subsidiaries: F&F Equipment, Inc. and Industrial Plating Enterprise Co.

F&F Equipment, Inc. (F&F) was incorporated on October 4, 1983 under the laws of the State of Florida. F&F was formed to engage principally in the "import, export, retail & wholesale of firearms equipment, ammunition & other devices and for the purpose of transacting any and/or all lawful business." F&F conducts its business operations under the assumed name of "American Ammunition."

In June 2002, American Ammunition, Inc. formed a wholly owned subsidiary, Industrial Plating Enterprise Co. (IPE), which started production on June 14, 2002. IPE is a fully licensed and approved electrochemical metallization facility with significant capacity for processing our line of projectiles as well as other products and services while employing environmentally sound water conservation and proven waste treatment techniques.

Results of Operations

Three months ended March 31, 2005 compared with the three months ended March 31, 2004.

During the three months ended March 31, 2005, we experienced aggregate net revenues of approximately \$1,170,000, as compared to approximately \$282,000 during the comparable quarter of 2004. The first quarter 2005 sales compare comparably to the 4th quarter 2004 sales of approximately \$1,535,000.

During the first quarter of 2004, the Company commenced a direct solicitation

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program for it's "dealer direct" sales program. As this endeavor has received a very positive initial response from the qualified retail resellers of the Company's product, the announcement of this program had a significantly detrimental impact on the Company's relationship with wholesale distributors and, accordingly, had a significant negative impact on first quarter 2004 sales.

The Company continues to experience high demand for small arms ammunition from both the retail channel market and domestic and foreign governments. The Company has identified certain production issues which has inhibited the full realization of existing product demands and has begun to take the necessary steps to add specific machinery to counteract these issues.

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We experienced costs of goods sold of approximately \$1,536,580 for the three months ended March 31, 2005 as compared to approximately \$705,000 for the three months ended March 31, 2004.

Through March 31, 2005, and subsequent thereto, we continue to experience negative trends off of our standard production costs for material and labor due to difficulties in training new employees, adding new products to our catalog and lower than expected orders during the first two quarters of 2004 due to uncontrollable delays in ordering by various U. S. Governmental entities. Management is of the opinion that the production labor force is stable and able to maintain a constant standard of quality for future periods. We experience variable costs in the area of material consumption and direct labor. We have recognized depreciation expense on production equipment of approximately \$190,000 and \$173,000, respectively, in the above cost of goods expense totals. These depreciation levels are anticipated to fluctuate nominally in future periods based upon either the full depreciation of older equipment and/or the addition of new equipment to expand capacity. For the three month periods ended March 31, 2005 and 2004, we generated a negative gross profit of approximately \$(366,000), or (31.3%), and approximately \$(424,000), or (150.5%). Based on orders received and products shipped during the first quarter of 2005 (through the filing date of this document) and our ongoing conversations with various customers, management continues to believe that the Company should be able to generate a positive gross profit in future periods..

We experienced nominal research and development expenses of approximately \$1,700 and \$-0-, respectively, during the respective three month periods ended March 31, 2005 and 2004, principally related to refinements in and the expansion of our product line.

During the first quarters of 2005 and 2004, we expended approximately \$81,000 and \$123,000, respectively, in advertising and marketing expenses, principally in developing and promoting our retail dealer direct program. We anticipate to continue our marketing efforts in this area in future periods; however, the volume and frequency of our expenditures may fluctuate as management allocates available capital to these efforts.

Other general and administrative expenses increased by approximately \$29,000 from approximately \$320,000 for the three months ended March 31, 2005 as compared to approximately \$291,000 for the three months ended March 31, 2004. These increases are not identifiable by one specific area; however, relate to general corporate expenses, office and administrative wages and salaries and other related office overhead.

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Included in our results of operations for the first quarter of 2004 are certain non-cash expenditure charges to operations of approximately \$321,000 for compensation expense related to common stock issuances at less than "fair value". The calculation of these charges result from our issuing common stock for either cash or services at valuations below the closing quoted market price of our common stock (as discounted, as applicable) and either the cash received or the value of the services provided to us by third parties.

We recognized a net loss of approximately \$(786,000) and \$(1,188,000) for the respective three month periods ended March 31, 2005 and 2004, respectively, or \$(0.01) and \$(0.02) per share.

Liquidity And Capital Resources

As of March 31, 2005, December 31, 2004 and March 31, 2004, respectively, we had working capital of approximately \$239,000, \$872,000 and \$1,533,000. Our working capital position continues to fluctuate based on collections on our trade accounts receivable and investments from the mandatory exercise of our outstanding warrant related to our convertible debenture. Further, we anticipate that we have sufficient inventory levels to support our retail dealer direct program and our existing and anticipated U. S. Government contracts.

We have used cash in operating activities of approximately \$(392,000) and \$(589,000) during the quarters ended March 31, 2005 and 2004, respectively.

The most significant use of cash in operations during the quarter ended March 31, 2004 was for the increase in on-hand inventory to support the anticipated demand on our retail dealer direct program and our existing and anticipated U. S. Government contracts.

We anticipate that our improved liquidity position will continue to improve as management is of the opinion that, with the current changes to our production capacity, the Company will be in a position to better support all

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existing orders and accept existing inquiries which have previously been denied due to the lack of production capacity and liquidity.

During the quarters ended March 31, 2005 and 2004, respectively, we added approximately \$36,000 and \$302,000 in new equipment. Based on communicated future demand for our products, we have instituted a program to expand our production capacity through the addition of additional equipment from the open market. The equipment ultimately to be added is fully dependent upon the Company's cash position, the availability of either new equity or debt capital and the ultimate realization of communicated future product sales demand. Management is of the opinion that sufficient demand will be present, as supported by new product development and increased product marketing efforts, to justify this expansion. However, we may not be able to obtain additional funding or, that such funding, if available, will be obtained on terms favorable to or affordable by us.

Convertible Debenture

The Company entered into a Securities Purchase Agreement with La Jolla Cove Investors, Inc. ("La Jolla") on October 4, 2002 for the sale of (i) \$250,000 in convertible debentures and (ii) warrants to buy 30,000,000 shares of our common stock. On March 13, 2003 and May 6, 2003, La Jolla advanced an aggregate of

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\$350,000 to our company which such funding was allocated towards the principal balance of our convertible debentures.

As of March 31, 2005, the outstanding balance on the convertible debenture is approximately \$266,365 and we have approximately 2,663,650 warrants outstanding.

The debentures bear interest at 8%, mature on June 30, 2006, and are convertible into our common stock, at the selling stockholder's option. The convertible debentures are convertible into the number of our shares of common stock equal to the principal amount of the debentures being converted multiplied by 11, less the product of the conversion price multiplied by 10 times the dollar amount of the debenture. The conversion price for the convertible debentures is the lesser of (i) \$1.00 or (ii) seventy six percent of the average of the five lowest volume weighted average prices during the twenty (20) trading days prior to the conversion. Accordingly, there is in fact no limit on the number of shares into which the debenture may be converted. However, in the event that our market price is less than \$.30, we will have the option to prepay the debenture at 125% rather than have the debenture converted. In addition, the selling stockholder is obligated to exercise the warrant concurrently with the submission of a conversion notice by the selling stockholder. As of December 31, 2004, the warrant is exercisable into 2,663,650 shares of common stock at an exercise price of \$1.00 per share.

In December 2004, we entered into an addendum to the convertible debenture and warrant whereby the Company agreed to the following:

- * the discount multiplier was reduced from eighty percent to seventy six percent;
- * within five business days after this registration statement being declared effective, La Jolla is required to submit a debenture conversion in the amount of \$10,000 and every ten business days thereafter La Jolla shall submit three additional debenture conversion in the amount of \$10,000 each;
- * within five business days after this registration statement being declared effective, La Jolla shall wire \$400,000 to us as a prepayment towards the exercise of its warrant; and
- * immediately following the sale of all shares held by La Jolla in connection with the debenture conversions in the aggregate amount of \$40,000, La Jolla shall wire \$275,000 to us as a prepayment towards the exercise of its warrant and shall submit a debenture conversion in the amount of \$6,250 on the first business day of each month until the debenture is no longer outstanding.

LaJolla has contractually agreed to restrict its ability to convert or exercise its warrants and receive shares of our common stock such that the number of shares of common stock held by them and their affiliates after such conversion or exercise does exceed 4.9% of the then issued and outstanding shares of common stock.

Due to the contractually agreed mandatory conversion of this Debenture, the Company has reflected this transaction in its balance sheet as a "mezzanine" level debt obligation on its balance sheet, between "Total Liabilities" and "Stockholders' Equity". Upon the respective mandatory conversion, the Company will relieve the respective portion of the Debenture and the any related accrued, but unpaid interest, and credit this amount to the respective "common stock" and "additional paid-in capital" accounts in the stockholder's equity section for the par value and excess amount over the par value of the respective shares issued.

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As the warrant is non-detachable from the Debenture and requires simultaneous exercise upon conversion of the Debenture, no value was assigned to the issued warrant. Upon exercise of the warrant, the Company will record the issuance of the underlying shares as a new issuance of common stock on the date of each respective exercise.

On various dates through December 31, 2003, the Debenture Holder elected to convert an aggregate \$208,635, through 24 separate transactions, in outstanding Debenture principal into restricted, unregistered common stock. This election caused the Company to issue 4,561,753 shares of restricted, unregistered common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 2,086,350 shares of the Company's restricted, unregistered common stock for gross proceeds of \$2,086,350.

On various dates between January 1, 2004 and December 31, 2004, the Debenture Holder elected to convert an aggregate \$150,000, through 6 separate transactions, in outstanding Debenture principal into registered common stock. This election caused the Company to issue 4,900,000 shares of common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 1,500,000 shares of the Company's common stock for gross proceeds of \$1,500,000. As of December 31, 2004, an aggregate of 1,000,000 shares of the Company's common stock have been issued by the Company and are being held in escrow by the Company's counsel pending receipt of the final \$150,000 from the Debenture Holder.

Item 3 - Controls and Procedures

As required by Rule 13a-15 under the Exchange Act, within the 90 days prior to the filing date of this report, the Company carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures. This evaluation was carried out under the supervision and with the participation of the Company's President, Chief Executive and Chief Financial Officer. Based upon that evaluation, the Company's President, Chief Executive and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective. There have been no significant changes in the Company's internal controls or in other factors, which could significantly affect internal controls subsequent to the date the Company carried out its evaluation.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in Company reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in Company reports filed under the Exchange Act is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure.

Part II - Other Information

Item 1 - Legal Proceedings

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None

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

None

Item 3 - Defaults on Senior Securities

None

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

None

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Item 5 - Other Information

None

Item 6 - Exhibits

| Exhibit # | Description |
|-----------|--|
| 31.1 * | Certification pursuant to Section 302 of Sarbanes-Oxley Act of 2002 |
| 32.1 * | Certification pursuant to Section 906 of Sarbanes-Oxley Act of 2002. |

* Filed herewith

SIGNATURES

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

American Ammunition, Inc.

Date: May 21, 2005

By: /s/ Andres F. Fernandez

Andres F. Fernandez
President, Chief Executive Officer
Chief Financial Officer and Director

