UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Amendment No. 1)

(Mark one)

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

For the quarterly period ended December 31, 2005

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 Number: 000-24248

AMERICAN TECHNOLOGY CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**87-0361799**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
15378 Avenue of Science, Ste 100, San Diego, California	**92128**
(Address of principal executive offices)	**(Zip Code)**

(858) 676-1112

(Registrant s telephone number, including area code)

13114 Evening Creek Drive South, San Diego, CA 92128

(Former address, if changed since last report)

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. x Yes ¨ No

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

The number of shares of Common Stock, $.00001 par value, outstanding on January 31, 2006 was 24,308,215

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EXPLANATORY NOTE

This Amendment No. 1 on Form 10-Q/A for American Technology Corporation for the fiscal quarter ended December 31, 2005, is being filed in connection with the following circumstances.

In the first quarter of fiscal year 2006, the composition of our reportable segments changed because the management of a particular end-customer group was transferred from the Government and Military Group to the Commercial Group. In accordance with the requirements of Statement of Financial Accounting Standards No. 131 Disclosures about Segments of an Enterprise and Related Information, our management determined that re-classifying the prior period information for comparison is required. This adjustment has no impact on the revenue or gross profits (loss) as reported for the current year business segment data. This adjustment also has no impact on our balance sheets, statements of operations, statements of cash flows or on previously reported revenue, net income, earnings per share, assets, liabilities, or stockholders equity.

Changes Reflected in this Form 10-Q/A

As a result of the reclassification, the disclosures in the following items related to the three months ended December 31, 2005 and 2004 have been revised:

Part I, Item 1 Financial Statements and Notes to Financial Statements

Note 2 Restatement of a Prior Period

Note 17 Business Segment Data

Part I, Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations

Reclassification of Financial Information

Results of Operations

Except for the foregoing reclass and clarified presentation, this Form 10-Q/A continues to describe conditions as presented in the Original Form 10-Q. Except in the sections identified above, this Form 10-Q/A does not reflect events occurring after the filing of the Original Form 10-Q, or modify or update those disclosures, including exhibits to the Form 10-Q affected by subsequent events. Information not affected by the restatement is unchanged and reflects the disclosures made at the time of the Original Form 10-Q. Accordingly, this Form 10-Q/A should be read in conjunction with filings made with the SEC subsequent to the filing of the Original Form 10-Q, including any amendments to those filings.

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AMERICAN TECHNOLOGY CORPORATION

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

American Technology Corporation

BALANCE SHEETS

	December 31, 2005	September 30, 2005
	(Unaudited)	
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 7,184,882	$ 10,347,779
Trade accounts receivable, less allowance of $125,000 for doubtful accounts for each period	1,758,472	880,276
Inventories, net of $514,979 and $691,206 reserve for obsolescence	1,615,616	1,799,447
Prepaid expenses and other	221,731	201,339
Total current assets	10,780,701	13,228,841
Equipment, net	542,403	606,871
Patents, net	1,323,236	1,373,158
Total assets	$ 12,646,340	$ 15,208,870
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 1,016,679	$ 1,985,353
Accrued liabilities:		
Payroll and related	362,010	476,331
Deferred revenue	488,782	395,833
Warranty reserve	331,708	248,981
Legal settlements		71,900
Other		30,003
Derivative warrant instrument	1,400	282,000
Capital lease, short-term portion	8,223	12,131
Total current liabilities	2,208,802	3,502,532
Long-Term Liabilities:		
Derivative warrant instrument	812,400	1,564,000
Total liabilities	3,021,202	5,066,532
Commitments and contingencies		
Stockholders equity		
Preferred stock, $0.00001 par value; 5,000,000 shares authorized: none issued and outstanding		
Common stock, $0.00001 par value; 50,000,000 shares authorized; 24,308,215 and 24,290,840 shares issued and outstanding respectively	243	243

Additional paid-in capital	61,809,611	61,556,295
Accumulated deficit	(52,184,716)	(51,414,200)
Total stockholders equity	9,625,138	10,142,338
Total liabilities and stockholders equity	$ 12,646,340	$ 15,208,870

See accompanying notes to interim financial statements.

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American Technology Corporation

STATEMENTS OF OPERATIONS

(Unaudited)

	For the three months ended December 31,	
	2005	**2004**
Revenues:		
Product sales	$ 1,839,969	$ 4,346,913
Contract and license	59,409	62,000
Total revenues	1,899,378	4,408,913
Cost of revenues	835,240	1,562,667
Gross profit	1,064,138	2,846,246
Operating expenses:		
Selling, general and administrative	2,375,124	1,946,588
Research and development	565,993	1,474,978
Total operating expenses	2,941,117	3,421,566
Loss from operations	(1,876,979)	(575,320)
Other income (expense):		
Interest income	74,623	10,941
Interest expense	(360)	(12,330)
Unrealized gain (loss) on derivative revaluation	1,032,200	(950,141)
Total other income (expense)	1,106,463	(951,530)
Net loss	(770,516)	(1,526,850)
Dividend requirements on convertible preferred stock		277,775
Net loss available to common stockholders	$ (770,516)	$ (1,804,625)
Net loss per share of common stock basic and diluted	$ (0.03)	$ (0.09)
Average weighted number of common shares outstanding	24,302,848	19,812,515

See accompanying notes to interim financial statements.

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American Technology Corporation

STATEMENTS OF CASH FLOWS

(Unaudited)

	For the three months ended December 31,	
	2005	**2004**
Increase (Decrease) in Cash		
Operating Activities:		
Net loss	$ (770,516)	$ (1,526,850)
Adjustments to reconcile net loss to net cash used in operations:		
Depreciation and amortization	111,972	111,401
Warranty provision	90,133	82,163
Inventory obsolescence	(176,228)	
Loss on disposition of asset	1,432	
Share-based compensation expense	188,376	268,503
Write-off of abandoned patents	20,385	
Unrealized (gain) loss gain on derivative revaluation	(1,032,200)	950,141
Amortization of debt discount		8,059
Changes in assets and liabilities:		
Trade accounts receivable	(878,196)	(2,675,193)
Inventories	360,059	(271,779)
Prepaid expenses and other	(20,393)	(35,887)
Accounts payable	(1,040,574)	627,163
Warranty reserve	(7,406)	(5,246)
Accrued liabilities	(51,374)	295,634
Net cash used in operating activities	(3,204,530)	(2,171,891)
Investing Activities:		
Purchase of equipment	(19,399)	(190,026)
Patent costs paid		(70,868)
Net cash used in investing activities	(19,399)	(260,894)
Financing Activities:		
Payments on capital lease	(3,908)	(2,639)
Proceeds from issuance of unsecured promissory notes		2,000,000
Proceeds from exercise of common stock warrants		85,000
Proceeds from exercise of stock options	64,940	
Net cash provided by financing activities	61,032	2,082,361
Net decrease in cash	(3,162,897)	(350,424)
Cash, beginning of period	10,347,779	4,178,968

Cash, end of period	$ 7,184,882	$ 3,828,544
Supplemental Disclosure of Cash Flow Information		
Cash paid for interest	$ 360	$ 563
Non-cash financing activities:		
Warrants issued for offering costs	$	$ 843,105
Warrants issued for debt financing	$	$ 723,000

See accompanying notes to interim financial statements.

American Technology Corporation

Notes to Interim Financial Statements (unaudited)

1. OPERATIONS

American Technology Corporation (the Company), a Delaware corporation, is engaged in design, development and commercialization of sound, acoustic and other technologies. The Company produces products based on its HyperSonic Sound (HSS), Long Range Acoustic Device (LRAD), NeoPlanar and other sound technologies.

The Company s principal markets for its proprietary sound reproduction technologies and products are in North America, Europe and Asia.

2. RESTATEMENT OF PRIOR PERIOD BUSINESS SEGMENT DATA

The prior period business segment data in Note 13 has been reclassified. In the first quarter of fiscal year 2006, the composition of the Company s reportable segments changed because the management of a particular end-customer group was transferred from the Government and Military Group to the Commercial Group. In accordance with the requirements of Statement of Financial Accounting Standards No. 131 Disclosures about Segments of an Enterprise and Related Information, management of the Company determined that re-classifying the prior period information for comparison is required. This adjustment has no impact on revenues and gross profit (loss) as reported for the current year business segment data. This adjustment also has no impact on the Company s balance sheets, statements of operations or statements of cash flows to the quarter ended December 31, 2005.

3. STATEMENT OF PRESENTATION AND MANAGEMENT S PLAN

The accompanying unaudited interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. In the opinion of management, the interim financial statements reflect all adjustments of a normal recurring nature necessary for a fair presentation of the results for interim periods. Operating results for the three month period are not necessarily indicative of the results that may be expected for the year. The interim financial statements and notes thereto should be read in conjunction with the Company s audited financial statements and notes thereto for the year ended September 30, 2005 included in the Company s annual report on Form 10-K. Certain amounts reported in prior periods have been reclassified to be consistent with the current period presentation.

We incurred net losses of $770,516 and $1,804,625 in the three months ended December 31, 2005 and 2004, respectively. We have substantial research and development and selling, marketing and general administrative expenses, and our margins from the sale of our products have not yet been sufficient to offset these costs. We expect to incur additional operating losses during fiscal 2006. Based on our cash position, and assuming currently planned expenditures and level of operations, we believe we have sufficient capital resources for the next twelve months. Our operating plans are based on us continuing to increase revenues and generate positive cash flows from operations. See Liquidity

and Capital Resources , below. If required, we have significant flexibility to adjust the level of research and development and selling and administrative expenses based on the availability of resources. However, reductions in expenditures could delay development and adversely affect our ability to generate future revenues.

4. NET LOSS PER SHARE

Basic net loss per share includes no dilution and is computed by dividing net loss available to common stockholders, after deduction for cumulative imputed and accreted dividends, by the weighted average number of common shares outstanding for the period. Diluted net loss per share reflects the potential dilution of securities

American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

that could share in the earnings of an entity. The Company s losses for the periods presented cause the inclusion of potential common stock instruments outstanding to be antidilutive. Stock options and warrants exercisable into 5,611,066 and 5,739,577 shares of common stock were outstanding at December 31, 2005 and 2004 respectively. These securities are not included in the computation of diluted net loss per share because of the losses, but could potentially dilute earnings per share in future periods.

Net loss available to common stockholders decreased to ($0.03) in the three months ended December 31, 2005 from ($0.09) in the three months ended December 31, 2004. In computing net loss per share, the net loss for the three months ended December 31, 2004 was increased $277,775 by imputed deemed dividends based on the value of warrants issued and the computed beneficial conversion amount of convertible preferred stock. Such non-cash imputed deemed dividends were not included in the Company s stockholders equity as the Company has an accumulated deficit and therefore were reflected as an increase and a related decrease to additional paid in capital. Amounts are included in net loss available to common stockholders. The imputed deemed dividends were not contractual obligations of the Company to pay such imputed dividends.

The provisions of each of the Company s series of preferred stock also provided for a 6% per annum accretion in the conversion value (similar to a dividend). Such accretions were not included in the Company s stockholders equity as the Company has an accumulated deficit and therefore they were reflected as an increase and a related decrease to additional paid in capital. These non-cash amounts also increased the net loss available to common stockholders. Net loss available to common stockholders is computed as follows:

	Three Months Ended December 31,	
	2005	2004
Net loss	$ (770,516)	$ (1,526,850)
Imputed deemed dividends on Series D and E warrants issued with preferred stock		(101,280)
Imputed deemed dividends on Series D and E preferred stock		(133,063)
Accretion on preferred stock at 6% stated rate:		
Series D preferred stock		(7,667)
Series E preferred stock		(35,765)
Net loss available to common stockholders	$ (770,516)	$ (1,804,625)

5. STOCK-BASED COMPENSATION

Share-Based Payments. In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123 (SFAS 123(R)), Share-Based Payment, which establishes accounting for share-based awards exchanged for employee services and requires companies to expense the estimated fair value of these awards over the requisite employee service period. In March 2005, the U.S. Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 which the Company has applied in the adoption of

SFAS 123(R). On April 14, 2005, the U.S. Securities and Exchange Commission adopted a new rule amending the effective dates for FAS 123R. In accordance with the new rule, the accounting provisions of SFAS 123(R) are effective for the Company beginning in the quarter ended December 31, 2005.

Under SFAS 123(R), share-based compensation cost is measured at the grant date, based on the estimated fair value of the award at that date, and is recognized as expense over the employee s requisite service period (generally over the vesting period of the award). The Company has no awards with market or performance conditions. The Company adopted the provisions of SFAS 123(R) on October 1, 2005, the first day of the Company s fiscal year 2006, using a modified prospective application, which provides for certain changes to the

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American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

method for valuing share-based compensation. Under the modified prospective application, prior periods are not revised for comparative purposes. The valuation provisions of SFAS 123(R) apply to new awards and to awards that are outstanding on the effective date and subsequently modified or cancelled. Estimated compensation expense for awards outstanding at the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under FASB Statement No. 123, Accounting for Stock-Based Compensation (FAS 123).

On November 10, 2005, FASB issued FASB Staff Position No. FAS 123(R)-3, Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards . We are considering whether to adopt the alternative transition method provided in the FASB Staff Position for calculating the tax effects of stock-based compensation pursuant to SFAS 123(R). The alternative transition method includes simplified methods to establish the beginning balance of the additional paid-in capital pool (APIC pool) related to the tax effects of employee stock-based compensation, and to determine the subsequent impact on the APIC pool and statements of cash flows of the tax effects of employee stock-based compensation awards that are outstanding upon adoption of SFAS 123(R).

Share-Based Compensation Information under SFAS 123(R)

The Company s employee stock options have various restrictions that reduce option value, including vesting provisions and restrictions on transfer and hedging, among others, and are often exercised prior to their contractual maturity. (Note 12)

Under the provisions of SFAS 123(R) we recorded $188,376 of stock compensation expense in our unaudited Statement of Operations for the three months ended December 31, 2005. A total of $149,673 of this expense relates to prior year awards vesting after October 1, 2005 and $38,703 relates to options granted after the adoption of SFAS 123(R). The weighted-average estimated fair value of employee stock options granted during the three months ended December 31, 2005 was $2.47 per share using the Black-Scholes option-pricing model with the following weighted-average assumptions (annualized percentages):

	Three Months Ended December 31, 2005
Volatility	67.0%
Risk-free interest rate	3.68%
Forfeiture Rate	5.0%
Dividend yield	0.0%
Expected Life in years	3.9

The dividend yield of zero is based on the fact that we have never paid cash dividends and have no present intention to pay cash dividends. Expected volatility is based on the historical volatility of our common stock over the period commensurate with the expected life of the options. The risk-free interest rate is based on observed and expected time to post-vesting exercise and forfeitures of options by our employees.

As share-based compensation expense recognized in the Statement of Operations for the first quarter of fiscal 2006 is based on awards ultimately expected to vest, it is reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Pre-vesting forfeitures were estimated to be approximately 5% in the first quarter of fiscal 2006 based on historical experience. Under the provisions of SFAS 123(R), we will record additional expense if the actual forfeiture rate is lower than we estimated, and will record a recovery of prior expense if the actual forfeiture is higher than we estimated. In the Company s pro forma information required under FAS 123 for the periods prior to fiscal 2006, the Company accounted for forfeitures as they occurred.

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American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

Since we have a net operating loss carryforward as of December 31, 2005, no excess tax benefit for the tax deductions related to stock-based awards were recognized in the Statement of Operations for the quarter ended December 31, 2005. Additionally, no incremental tax benefits were recognized from stock options exercised in the quarter ended December 31, 2005 which would have resulted in a reclassification to reduce net cash provided by operating activities with an offsetting increase in net cash provided by financing activities.

As of December 31, 2005, there was $2.5 million of total unrecognized compensation cost related to non-vested share-based employee compensation arrangements. The cost is expected to be recognized over a weighted-average period of 3.5 years.

Pro Forma Information under FAS 123 for Periods Prior to Fiscal 2006

Prior to adopting the provisions of SFAS 123(R), the Company recorded estimated compensation expense for employee stock options based upon their intrinsic value on the date of grant pursuant to Accounting Principles Board Opinion 25 (APB 25), Accounting for Stock Issued to Employees and provided the required pro forma disclosures of FAS 123. Because the Company established the exercise price based on the fair market value of the Company s stock at the date of grant, the stock options had no intrinsic value upon grant, and therefore no estimated expense was recorded prior to adopting SFAS 123R.

For purposes of pro forma disclosures under SFAS 123 for the three months ended December 31, 2004, the estimated fair value of the stock options was assumed to be amortized to expense over the stock options vesting periods. The pro forma effects of recognizing estimated compensation expense under the fair value method on net loss and loss per common share for the three months ended December 31, 2004 were as follows:

	Three Months Ended December 31, 2004
Net loss, as reported	$ (1,804,625)
Add: Stock-based employee compensation expense included in reported net loss	268,503
Deduct: Share-based employee compensation expense determined using the fair value based method	(559,242)
Pro forma net loss available to common stockholders	$ (2,095,364)
Earnings per common share:	
Basic and diluted as reported	$ (0.09)
Basic and diluted pro forma	$ (0.11)

The pro forma effects of estimated share-based compensation expense on net income and earnings per common share for the three months ended December 31, 2004 were estimated at the date of grant using the Black-Scholes option-pricing model based on the following assumptions (annualized percentages):

	Three Months Ended December 31, 2004
Volatility	56.0%
Risk-free interest rate	2.97%
Forfeiture Rate	5.0%
Dividend yield	0.0%
Expected Life in years	2.5

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American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

6. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2005, the (FASB) issued SFAS No. 154, Accounting Changes and Error Corrections , applying to all voluntary accounting principle changes as well as the accounting for and reporting of such changes. SFAS No. 154 replaces APB Opinion No. 20, Accounting Changes , and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company does not expect SFAS No. 154 to affect the Company s financial condition or results of operations.

In March 2005, the FASB issued Interpretation No. 47 (FIN 47), Accounting for Conditional Asset Retirement Obligations. FIN 47 clarifies that an entity must record a liability for a conditional asset retirement obligation if the fair value of the obligation can be reasonably estimated. The provision is effective no later than the end of fiscal years ending after December 15, 2005. The Company has determined that FIN 47 has no effect on the Company s operations at this time.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Non-monetary Assets, an Amendment of APB Opinion No. 29 , which is effective for non-monetary exchanges occurring in fiscal periods beginning after June 15, 2005. SFAS No. 153 amends APB Opinion No. 29, Accounting for Non-monetary Transactions to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. A non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. The Company does not expect SFAS No. 153 to affect the Company s financial condition or results of operations.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB 43, Chapter 4. SFAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. SFAS No. 151 is effective for fiscal years beginning after June 15, 2005. The Company has determined that SFAS No. 151 has no effect on the Company s operations and financial condition at this time.

7. INVENTORIES AND CONTRACT MANUFACTURING

Inventory is stated at the lower of cost, which approximates actual costs on a first in, first out cost basis, or market.

Inventories consisted of the following:

	December 31, 2005	September 30, 2005
Finished goods	$ 436,195	$ 790,707
Work in process	191,504	
Raw materials	1,502,895	1,699,946
	2,130,594	2,490,653
Reserve for obsolescence	(514,979)	(691,206)
	$ 1,615,616	$ 1,799,447

Included in inventory are $188,483 and $148,826 of raw materials located at contract manufacturing locations at December 31, 2005 and September 30, 2005, respectively.

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American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

8. MAJOR CUSTOMERS

For the three months ended December 31, 2005, revenues from one customer accounted for 66% of revenues and revenues from another customer accounted for 12% of total revenues. For the three months ended December 31, 2004, revenues from two customers accounted for 75% and 15% of revenues with no other single customer accounting for more than 10% of revenues.

At December 31, 2005, accounts receivable from two customers accounted for 56% and 12% of total accounts receivable with no other single customer accounting for more than 10% of the accounts receivable balance. At September 30, 2005, accounts receivable from two customers accounted for 18% and 14% of total accounts receivable with no other single customer accounting for more than 10% of the accounts receivable balance.

9. INTANGIBLES

Patents are carried at cost and, when granted, are amortized over their estimated useful lives. The carrying value of patents is periodically reviewed and impairments, if any, are recognized when the expected future benefit to be derived from an individual intangible asset is less than its carrying value. Patents consisted of the following:

	December 31, 2005	September 30, 2005
Cost	$ 1,772,234	$ 1,792,619
Accumulated amortization	(448,998)	(419,461)
Net patent	$ 1,323,236	$ 1,373,158

10. PRODUCT WARRANTY COST

The Company establishes a warranty reserve based on anticipated warranty claims at the time product revenue is recognized. Factors affecting warranty reserve levels include the number of units sold and anticipated cost of warranty repairs and anticipated rates of warranty claims. The Company evaluates the adequacy of the provision for warranty costs each reporting period.

Changes in the warranty reserve during the three months ended December 31, 2005 and 2004 were as follows:

	Three Months Ended December 31,	
	2005	**2004**
Beginning balance	$ 248,981	$ 331,917
Warranty provision	90,133	82,163
Warranty payments	(7,406)	(5,246)
Ending balance	$ 331,708	$ 408,834

In the fiscal quarter ended December 31, 2005, we increased our reserve for potential warranty claims related to our HSS 450 product by $63,470 as a result of discovering possible deficiencies in the manufacturing process for manufacturing these units. This additional reserve was computed based on the number of HSS 450

American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

units previously sold and under warranty. We believe we have corrected these manufacturing deficiencies. Future warranty costs could further adversely affect our financial position, results of operations and business prospects.

11. DERIVATIVE FINANCIAL INSTRUMENTS

In December 2004, the Company entered into a common stock purchase agreement, registration rights agreement and warrant as part of a Committed Equity Financing Facility (CEFF) that was subsequently terminated in July 2005 with no shares issued. As part of the arrangement, the Company issued a warrant to purchase 275,000 shares of its common stock at a price of $8.60 per share. As the warrant was initially unregistered, and did not specify how it would be settled prior to registration, the warrant was initially reported as a liability of $843,103 in accordance with Emerging Issues Task Force (EITF) 00-19 Accounting for Derivative Financial Instruments, Indexed to, and Potentially Settled in a Company s Own Stock. The following variables were used to determine the fair value of the warrant under the Black-Scholes option pricing model: volatility of 56%, term of 5.5 years, risk free interest of 2.97% and underlying stock price equal to fair market value at the time of issuance. The value was recorded as prepaid transaction costs. The warrants were revalued

each period as non-cash income or expense and an unrealized loss on derivative revaluation of $950,141 was recorded for the three months ended December 31, 2004. As the warrants were cancelled in July 2005 there is no derivative liability at September 30, 2005 or thereafter related to this transaction.

In July 2005, the Company entered into a common stock purchase agreement, registration rights agreement and warrants in connection with a common stock equity financing. In connection with the financing, the Company issued warrants to purchase an aggregate of 1,581,919 shares of common stock. The Company accounted for the value of the warrants as a deemed liability in accordance with the interpretive guidance in EITF Issue No. 05-4. The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument Subject to EITF Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock . The consensus of EITF Issue No. 05-4 has not been finalized. The aggregate liability at issuance was $2,896,000 using the following variables under the Black-Scholes option pricing model: volatility of 59%, term of each warrant, risk free interest rate of 3.53% and 3.95% and underlying stock price equal to fair market value at the time of issuance. EITF Issue 00-19 also requires the Company to revalue the warrants as a derivative instrument periodically in connection with changes in the underlying stock price and other assumptions, with the change in value recorded as non-cash income or expense. At September 30, 2005, there was an unrealized gain of $1,050,000 to reflect the change in value of the warrants from issuance reducing the liability to $1,846,000 ($282,000 current and $1,564,000 long-term). At December 31, 2005 there was a further unrealized gain of $1,032,200 to reflect the change in value of the warrants for the three months ended December 31, 2005 reducing the liability to $813,800 ($1,400 current and $812,400 long-term) using a volatility of 67% and 59%, term of each warrant, risk free interest rate of 4.39% and 3.97% and underlying stock price equal to fair market value.

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American Technology Corporation

Notes to Interim Financial Statements (unaudited) (Continued)

12. STOCKHOLDERS EQUITY

Summary

The following table summarizes changes in equity components from transactions during the three months ended December 31, 2005:

	Common Stock				
	Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders Equity (Deficit)
Balance, September 30, 2005	24,290,840	$ 243	$ 61,556,295	$ (51,414,200)	$ 10,142,338
Issuance of common stock:					
Upon exercise of stock options	17,375		64,940		64,940
Stock Option Compensation Expense			188,376		188,376
Net loss for the period				(770,516)	(770,516)
Balance, December 31, 2005	24,308,215	$ 243	$ 61,809,611	$ (52,184,716)	$ 9,625,138

Stock Options

During the three months ended December 31, 2005, non-cash compensation expenses was $188,376 under SFAS No. 123(R) (See Note 5). During the three months ended December 31, 2004, the Company recorded non-cash compensation expense of $266,963 for the extension of time to exercise stock options for former employees relating to an aggregate of 92,675 shares of common stock, and $1,540 of non-cash compensation expense for the value of options granted to non-employees. These options were valued in the same manner as described in Note 4 for employee options.

As of December 31, 2005, we had three equity incentive plans. The 2005 Equity Incentive Plan (2005 Equity Plan), authorizes for issuance as stock options, stock appreciation rights, or stock awards an aggregate of 1,500,000 new shares of common stock to employees, directors or consultants. The reserve under the 2005 Equity Plan will include any shares subject to options under the Company s prior plans that expire or become unexercisable for any reason without having been exercised in full. As a result of the effectiveness of the 2005 Equity Plan, the 2002

Plan is no longer available for new option grants.

At the effective date of the 2005 Equity Plan, approximately 1,660,811 shares were subject to option under prior plans. The total plan reserve, including the new shares and shares currently reserved under prior plans, allows for the issuance of up to 3,312,501 shares. At December 31, 2005, there were options outstanding covering 698,000 shares of common stock under the 2005 Equity Plan.

The 2002 Plan reserved for issuance 2,350,000 shares of common stock. The 2002 Plan was terminated with respect to new grants in April 2005 but remains in effect for grants prior to that time. At December 31, 2005, there were options outstanding covering 736,538 shares of common stock under the 2002 Plan. The Company s 1997 Stock Option Plan (1997 Plan) reserved for issuance 1,000,000 shares of common stock. The 1997 Plan was terminated with respect to new grants in August 2002, but remains in effect for grants prior to that time.

Shares subject to options under the 1997 Plan or the 2002 Plan that expire, are cancelled or are terminated without being exercised, become available for future grants under the 2005 Equity Plan. At September 30, 2005, there were options outstanding covering 292,000 shares of common stock under the 1997 plan.

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Other Employee Stock Options

The Company has granted options outside the above plans as inducements to employment to new employees. At December 31, 2005, there were options outstanding covering 306,875 shares of common stock from grants outside the stock option plans.

Options awards are generally granted with an exercise price equal to the fair market value of our common stock at the grant date and have 10-year contractual terms. Options awards typically vest in accordance with one of the following schedules:

a. 25% of the option shares vest and become exercisable on the first anniversary of the grant date and the remaining 75% of the option shares vest and become exercisable quarterly in equal installments thereafter over three years

b. Option shares vest and become exercisable quarterly in equal installments over four years

Certain option awards provide for accelerated vesting if there is a change in control (as defined in the Plans).

The following table summarizes information about stock option activity during the three months ended December 31, 2005:

	Number of Shares		Weighted Average Exercise Price
Outstanding October 1, 2005	2,070,810	$	4.43
Granted	453,000	$	4.73
Canceled/expired	(473,022)	$	6.60
Exercised	(17,375)	$	3.74
Outstanding December 31, 2005	2,033,413	$	5.28
Exercisable December 31, 2005	966,765	$	4.46

Options outstanding are exercisable at prices ranging from $2.50 to $10.06 and expire over the period from 2005 to 2010 with an average life of 3.27 years.

Stock Purchase Warrants

The following table summarizes information about warrant activity during the three months ended December 31, 2005:

	Warrants		
	Number of Shares	Weighted Average Exercise Price	
Outstanding October 1, 2005	3,577,653	$	5.11
Issued		$	
Exercised		$	
Canceled/expired		$	
Outstanding December 31, 2005	3,577,653	$	5.11

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At December 31, 2005, the following stock purchase warrants were outstanding arising from offerings and other transactions:

Number	Exercise Price	Expiration Date
864,706	$7.23	March 28, 2006
617,500	$2.00	September 30, 2006
451,880	$3.01	March 31, 2007
272,729	$6.55	July 10, 2007
100,000	$4.25	September 30, 2007
353,625	$3.25	December 31, 2007
50,000	$3.63	April 8, 2008
717,213	$6.36	July 18, 2009
75,000	$8.60	December 31, 2009
75,000	$9.28	December 31, 2009
3,577,653		

The $3.01 warrants, the $3.25 warrants, the $6.36 warrants, the $6.55 warrants and the $7.23 warrants contain certain antidilution rights if the Company sells securities for less than the exercise price.

13. BUSINESS SEGMENT DATA

The Company is engaged in design, development and commercialization of sound, acoustic and other technologies. The Company s operations are organized into two segments by the end-user markets they serve. The Company s reportable segments are strategic business units that sell the Company s products into distinct markets. The Commercial Products Group (Commercial Group) markets and licenses LRAD, HSS, NeoPlanar and other sound products incorporating the Company s technologies to customers and end users that employ audio in consumer, commercial cruise ship security and other business applications. The Government and Force Protection Systems Group (Government and Military Group) markets LRAD, MRAD and NeoPlanar products to government and military customers and to the expanding force protection and police and similar private security markets. The segments are managed separately because each segment requires different selling and marketing strategies as the class of customers within each segment is different. Effective October 1, 2005, the Company changed the composition of its two reportable business segments to reflect that management had shifted responsibility for the cruise ship end-user category from the Government and Military Group to the Commercial Group. For the three months ended December 31, 2004, sales to cruise ship customers were included in the Government Group, but have been reclassified to the Commercial Group to be consistent with the current period presentation.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company does not allocate operating expenses or assets between its two reportable segments. Accordingly the measure of profit for each reportable segment is gross profit.

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Summarized below are the revenues and gross profit (loss) for our business units:

	Three Months Ended December 31,		
	2005	**As Previously Reported 2004**	**As Restated 2004**
Revenues:			
Commercial Group	$ 1,304,473	$ 187,349	$ 852,349
Government and Military Group	594,905	4,221,564	3,556,564
Total revenues	$ 1,899,378	$ 4,408,913	$ 4,408,913

	Three Months Ended December 31,		
	2005	**As Previously Reported 2004**	**As Restated 2004**
Gross profit (loss):			
Commercial Group	$ 805,216	$ (221,778)	$ 263,672
Government and Military Group	258,922	3,068,024	2,582,574
Total gross profit	$ 1,064,138	$ 2,846,246	$ 2,846,246

14. LITIGATION

The Company may at times be involved in litigation in the ordinary course of business. The Company will also, from time to time, when appropriate in management s estimation, record adequate reserves in the Company s financial statements for pending litigation. Currently, there are no pending material legal proceedings to which the Company is a party or to which any of its property is subject.

15. INCOME TAXES

At December 31, 2005, a valuation allowance has been provided to offset the net deferred tax asset as management has determined that it is more likely than not that the deferred tax asset will not be realized. At September 30, 2005 the Company had for federal income tax purposes net operating loss carryforwards of approximately $46,972,000, which expire through 2026 of which certain amounts are subject to significant limitations under the Internal Revenue Code of 1986, as amended.

16. LEASE FOR PRINCIPAL FACILITIES

In December 2005, the Company entered into a sublease agreement with Anacomp, Inc., as sublandlord, to sublease approximately 23,698 square feet of office, warehousing, product assembly, and research space located at 15378 Avenue of Science, San Diego, California 92118. The sublease is for a term commencing January 1, 2006 and expiring May 31, 2011. The agreement provides for a monthly expense of $29,622.50 (representing $1.25 per rentable square foot) during the term. In addition to the monthly base rental expense, the Company will be responsible for certain costs and charges specified in the sublease, including the Company s proportionate share of the building operating expenses and real estate taxes. Costs associated with this move are estimated to be approximately $260,000, which amount includes approximately $194,000 of leasehold improvements.

In addition, the sublease provides that the Company has a right of first refusal on additional space in the building, which contains a total of 68,910 square feet including the Company s premises. Anacomp will also provide a $10,000 tenant improvement allowance towards the completion of lobby improvements and a $50,000

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Notes to Interim Financial Statements (unaudited) (Continued)

letter of credit in the Company s favor which the Company may draw upon to the extent necessary to offset any increase in our rent or relocation costs that is incurred due to Anacomp s failure to maintain the lease with the master landlord for the building.

17. SUBSEQUENT EVENTS

In January 2006, the Company extended the lease for its current facility at 13114 Evening Creek Drive South, San Diego, California 92128 for one month to February 28, 2006.

In January 2006, the Company entered into a lease agreement with Priority Properties LLC, to lease approximately 1,700 square feet of office space located in Topsham, Maine, which will be used as a sales office for the Government and Military Group. The lease is for 12 months and can be renewed for up to five years.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the accompanying unaudited interim financial statements and the related notes included under Item 1 of this Quarterly Report on Form 10-Q, together with 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 September 30, 2005.

The following discussion provides an overview of our results of operations for the three months ended December 31, 2005 and 2004. Significant period-to-period variances in the statements of operations are discussed under the caption Results of Operations. Our financial condition and cash flows are discussed under the caption Liquidity and Capital Resources.

Forward Looking Statements

This report contains certain statements of a forward-looking nature relating to future events or future performance. Words such as expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions or variations of such words are intended to identify forward-looking statements, but are not the only means of identifying forward-looking statements. Prospective investors are cautioned that such statements are only predictions and that actual events or results may differ materially. In evaluating such statements, prospective investors should specifically consider various factors identified in this report, including any matters set forth under Part II, Item 1A (Risk Factors) of this report and under the caption Risk Factors in our Annual Report on Form 10-K, which cou