

Edgar Filing: SYNERGX SYSTEMS INC - Form 10QSB

SYNERGX SYSTEMS INC  
Form 10QSB  
May 12, 2004

U.S. SECURITIES AND EXCHANGE  
COMMISSION  
Washington, D. C. 20549

FORM 10-QSB

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the fiscal quarter ended March 31, 2004  
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TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT  
For the transition period from to

Commission file number 0-17580  
-----

SYNERGX SYSTEMS INC.

(Exact name of small business issuer as specified in its charter)

Delaware

11-2941299  
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(State or jurisdiction of incorporation or (IRS employer identification Number)  
organization)

209 Lafayette Drive, Syosset, New York 11791  
(Address of Principal Executive Offices) (Zip code)

(516) 433-4700  
(Issuer's telephone number)

Check whether the issuer (1) has filed all reports required to be filed by  
Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for  
such shorter period that 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: As of May 12, 2004, 4,756,862 shares  
of Registrant's Common Stock were issued and outstanding.

Transitional Small Business Disclosure Format (check one) Yes No

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### Part I - FINANCIAL INFORMATION

#### SYNERGX SYSTEMS INC. AND SUBSIDIARIES

#### CONDENSED CONSOLIDATED BALANCE SHEET (Unaudited)

	March 31, 2004
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	\$ 351,748
Accounts receivable, principally trade, less allowance for doubtful accounts of \$411,541	5,821,865
Inventories	3,121,063
Deferred taxes	315,000
Prepaid expenses and other current assets	598,132
TOTAL CURRENT ASSETS	10,207,808
PROPERTY AND EQUIPMENT -at cost, less accumulated depreciation and amortization of \$1,443,382	363,354
OTHER ASSETS	689,192
TOTAL ASSETS	\$11,260,354

See accompanying Notes to the Condensed Consolidated Financial Statements

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SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEET  
(Unaudited)

March 31,  
2004

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES

Notes and capital leases payable - current portion	\$ 34,323
Accounts payable and accrued expenses	3,087,855
Deferred revenue	409,253
	-----
TOTAL CURRENT LIABILITIES	3,531,431

Note payable to bank	1,845,676
Notes and capital leases payable - less current portion	33,377
Deferred taxes	20,300
	-----
TOTAL LIABILITIES	5,430,784

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY

Preferred stock, 2,000,000 shares authorized- none issued and outstanding	
Common stock, 10,000,000 shares authorized, \$.001 par value; issued and outstanding 4,747,528 shares	4,747
Capital in excess of par	6,400,825
Accumulated deficit	(576,002)
	-----
TOTAL STOCKHOLDERS' EQUITY	5,829,570

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$11,260,354
	=====

See accompanying Notes to the Condensed Consolidated Financial Statements

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)

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	For the Three Months Ended March 31, 2004	2003
	-----	-----
Product sales	\$4,160,318	\$3,513,724
Subcontract sales	64,600	172,284
Service revenue	1,165,253	1,102,756
	-----	-----
Total revenues	5,390,171	4,788,764
	-----	-----
Cost of product sales	2,815,526	2,271,933
Cost of subcontract sales	54,153	145,194
Cost of service	837,695	782,136
Selling, general and administrative	1,507,778	1,406,716
Interest expense	21,125	17,274
Depreciation and amortization	40,004	42,896
Loss on equity investment	12,000	-
	-----	-----
	5,288,281	4,666,149
	-----	-----
Income before provision for income taxes	101,890	122,615
	-----	-----
Provision for income taxes:		
Current	34,400	64,000
Deferred	8,600	(3,000)
	-----	-----
	43,000	61,000
	-----	-----
Net Income	\$ 58,890	\$ 61,615
	=====	=====
Earnings per common share		
Basic earnings per share	\$0.01	\$0.02
	=====	=====
Diluted earnings per share	\$0.01	\$0.01
	=====	=====
Weighted average number of common shares outstanding	4,718,991	3,748,850
Weighted average number of common and dilutive common shares outstanding	5,178,703	4,250,784

See accompanying Notes to the Condensed Consolidated Financial Statements

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)

For the Six Months Ended March 31,  
2004

2003

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Product sales	\$7,179,266	\$6,805,029
Subcontract sales	143,535	443,183
Service revenue	2,269,176	2,178,071
	-----	-----
Total revenues	9,591,977	9,426,283
	-----	-----
Cost of product sales	4,918,277	4,535,416
Cost of subcontract sales	119,668	355,708
Cost of service	1,634,977	1,509,897
Selling, general and administrative	2,870,519	2,735,859
Interest expense	40,495	27,392
Depreciation and amortization	88,447	87,574
Loss on equity investment	32,000	
	-----	-----
	9,704,383	9,251,846
	-----	-----
(Loss) Income before provision for (benefit from) income taxes	(112,406)	174,437
	-----	-----
(Benefit from) Provision for income taxes:		
Current	(27,800)	88,000
Deferred	(17,200)	3,000
	-----	-----
	(45,000)	91,000
	-----	-----
Net (Loss) Income	\$ (67,406)	\$ 83,437
	=====	=====
Earnings Per Common Share		
Basic (Loss) Earnings Per Share	(\$0.02)	\$0.02
	=====	=====
Diluted (Loss) Earnings Per Share	(\$0.01)	\$0.02
	=====	=====
Weighted average number of common shares outstanding	4,441,037	3,748,850
Weighted average number of common and dilutive common share equivalents outstanding	5,129,795	4,115,266

See accompanying Notes to the Condensed Consolidated Financial Statements

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	For the Six Months Ended M	2
	2004	-----
OPERATING ACTIVITIES		
Net (loss) income	\$ (67,406)	\$ 8
Adjustments to reconcile net (loss) income to net cash		

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(used in) provided by operating activities:		
Depreciation and amortization	88,447	8
Deferred (benefit) tax	(17,200)	
Provision for doubtful accounts	-	(1
Loss on equity investment	32,000	
Changes in operating assets and liabilities:		
Accounts receivable	(27,944)	68
Inventories	(672,493)	(44
Prepaid expenses and other current assets	(209,936)	(24
Other assets	(25,204)	(2
Accounts payable and accrued expenses	161,591	6
Deferred revenue	(25,638)	(2
<hr style="border-top: 1px dashed black;"/>		
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES	(763,783)	15
<hr style="border-top: 1px dashed black;"/>		
INVESTING ACTIVITIES		
Purchases of property and equipment	(30,004)	(10
<hr style="border-top: 1px dashed black;"/>		
NET CASH USED IN INVESTING ACTIVITIES	(30,004)	(10
<hr style="border-top: 1px dashed black;"/>		
FINANCING ACTIVITIES		
Principal payments on notes payable and capital lease obligations	(89,435)	(8
Payments and proceeds from revolving line of credit - net	590,174	4
Proceeds from exercise of stock options and warrants	351,610	
<hr style="border-top: 1px dashed black;"/>		
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	852,349	(3
<hr style="border-top: 1px dashed black;"/>		
NET INCREASE IN CASH AND CASH EQUIVALENTS	58,562	2
Cash and cash equivalents at beginning of period	293,186	20
<hr style="border-top: 1px dashed black;"/>		
Cash and cash equivalents at end of period	351,748	22
<hr style="border-top: 3px double black;"/>		
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid during the period for:		
Income taxes	\$ 130,519	\$ 1
Interest	\$ 48,277	\$ 2

### SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:

During the six months ended March 31, 2004 and 2003, the Company incurred no capital lease obligations for the acquisition of equipment.

See accompanying Notes to the Condensed Consolidated Financial Statements

## SYNERGX SYSTEMS INC. AND SUBSIDIARIES

### NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

#### 1. BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in accordance

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with accounting principles generally accepted in the United States of America for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary in order to make the financial statements not misleading have been included. Results for the three and six months ended March 31, 2004 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in Synergx Systems Inc. ("Synergx" or "the Company") and Subsidiaries' annual report on Form 10-KSB for the year ended September 30, 2003.

### 2. REVENUE RECOGNITION

Product sales include sale of systems, which are similar in nature, that involve fire alarm, life safety and security (CCTV and card access), transit (on board systems) and communication (paging, announcement and audio/visual). Product sales represent sales of product along with the integration of technical services at a fixed price under a contract with an electrical contractor or end user customer or customer agent. Product sales are allocated using a constant gross profit percentage over the entire contract, and recognized, using the percentage-of-completion method of accounting. The Company utilizes a units-of-work performed method to measure progress towards completion of the contract. The effects of changes in contract terms are reflected in the accounting period in which they become known. Contract terms provide for billing schedules that differ from revenue recognition and give rise to costs and estimated profits in excess of billings, and billings in excess of costs and estimated profits. Costs and estimated profits in excess of billing were not material at March 31, 2004 and 2003 and have been included in accounts receivable. There were no billing in excess of costs and estimated profits at March 31, 2004 and 2003.

Subcontract sales principally represents revenue related to electrical installation of wiring and piping performed by others for the Company when the Company acts as the prime contractor and sells its products along with electrical installation. Subcontract revenue is also recognized during the entire project using the percentage-of-completion method of accounting as electrical installation is performed at the job site.

Service revenue from separate maintenance contracts is recognized on a straight-line basis over the terms of the respective contract, which is generally one year. Non-contract service revenue is recognized when services are performed.

## SYNERGX SYSTEMS INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

### 3. INVENTORIES

Inventories are priced at the lower of cost (first-in, first-out) or market and consist primarily of raw materials.

### 4. LONG TERM DEBT

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On October 9, 2003, the Company entered into a new \$3 million revolving credit facility with Hudson United Bank (the "Credit Facility"). The Credit Facility has an interest rate of prime plus 1/4% on outstanding balances (4.25% at March 31, 2004) and expires in October 2005. The Credit Facility is secured by all assets of the Company and all of its operating subsidiaries. Advances under this Credit Facility are measured against a borrowing base calculated on eligible receivables and inventory.

Initial proceeds from the new Credit Facility were used to pay off a former credit facility with Citizens Business Credit. At March 31, 2004 the full amount of the Credit Facility was available under the borrowing base calculation and \$1,846,000 was outstanding under this facility.

The Credit Facility includes certain restrictive covenants, which among other things, impose limitations on declaring or paying dividends, acquisitions, and capital expenditures. The Company is also required to maintain certain financial ratios and tangible net worth covenants. At March 31, 2004 the Company was not in default with any of its financial covenants.

### 5. EXERCISE OF WARRANTS AND STOCK OPTIONS

Mirtronics the largest stockholder of the Company had outstanding warrants to purchase 620,000 shares of the Company's Common Stock, which were issued in 1998, and were exercisable at any time until December 31, 2003 at an exercise price of \$.51 per share. Mirtronics exercised these warrants in December 2003 for a total consideration of \$316,200.

During the six months ending March 31, 2004, employee stock options to purchase 66,384 shares of Common Stock were exercised for a total consideration of \$35,410.

## SYNERGX SYSTEMS INC. AND SUBSIDIARIES

### NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

### 6. EARNINGS (LOSS) PER SHARE

The Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 128 "Earnings Per Share" which requires companies to report basic and diluted earnings per share ("EPS") computations. Basic EPS excludes dilution and is based on the weighted-average common shares outstanding and diluted EPS gives effect to potential dilution of securities that could share in the earnings of the Company. Diluted EPS reflects the assumed issuance of shares with respect to the Company's employee stock option plan and warrants. The Company did not have stock based compensation for the three and six months ended March 31, 2004 or 2003.

	Three Months ended March 31,		Six
Basic EPS Computation	2004	2003	2004

Net Income (Loss) available to common



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stockholders	\$ 58,890	\$ 61,615	\$ (67,40
Weighted average outstanding shares	4,718,991	3,748,850	4,441,03
Basic EPS (Loss)	\$.01	\$.02	\$ (.02
	=====	=====	=====
 Diluted EPS Computation			
Net Income (Loss) available to common stockholders	\$ 58,890	\$ 61,615	\$ (67,40
	=====	=====	=====
Weighted-average shares-basic	4,718,991	3,748,850	4,441,03
	-----	-----	-----
Plus: Incremental shares from assumed conversions			
Employee Stock Options	147,680	96,134	153,70
Warrants	312,032	405,800	535,05
	-----	-----	-----
Dilutive potential common shares	459,712	501,934	688,75
	-----	-----	-----
Adjusted weighted average shares diluted	5,178,703	4,250,784	5,129,79
	-----	-----	-----
Diluted EPS (Loss)	\$.01	\$.01	\$ (.0
	=====	=====	=====

### SYNERGX SYSTEMS INC. AND SUBSIDIARIES

#### NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

#### 7. INVESTMENT IN SECURE 724 L.P.

On May 29, 2003, the Company (through a special purpose Nova Scotia subsidiary) acquired 25% of the equity of Secure 724 LP ("Secure 724 LP"), an Ontario limited partnership, from Nafund Inc. ("Nafund") in consideration of (a) 300,000 shares of Common Stock; (b) warrants to purchase 50,000 shares of Common Stock at \$1.15 per share for 24 months; (c) agreeing to provide secured loans of up to Cdn\$300,000 (which was approximately \$229,000 U.S. at March 31, 2004) to Secure 724 LP pro rata with equity/loans to be provided by Nafund and tied to certain development milestones and (d) 150,000 shares of Common Stock to be issued in the future upon Secure 724 LP satisfying the milestones and Nafund providing the funding. Either the Company and/or Nafund can elect not to provide all or any part of the above funding (regardless of whether the milestones are attained). If milestones are attained and either the Company and/or Nafund elects not to provide all or part of the above funding it would have its equity reduced based on a formula.

The 25% investment in Secure 724 L.P. for 300,000 shares of Common Stock and warrants to purchase 50,000 shares of Common Stock was valued at \$432,500. This investment is accounted for utilizing the equity method and is included in OTHER ASSETS. The underlying equity of this investment on the date of the transaction was approximately \$73,000; resulting in goodwill of approximately \$359,500; which will not be amortized but will be tested for impairment. For the three and

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six months ended March 31, 2004, a \$12,000 and \$32,000, respectively, adjustment to the equity investment was recorded to reflect the Company's 25% portion of the operating loss of Secure 724 LP.

In connection with initial capital contribution per the partnership agreement, the Company advanced \$18,158 (Cdn\$25,000) to Secure 724 LP in May 2003 and upon reaching milestones advanced \$125,089 (Cdn\$175,000) in August 2003. These notes receivable bear interest at a rate of 4% and mature in May 2006 and August 2006, respectively.

This transaction was submitted to the stockholders of Synergx (as two directors of Synergx are directors of Secure 724 LP) and approved at its Annual Meeting on March 26, 2003.

There can be no assurance that the investment in Secure 724 LP will be profitable.

### 8. OTHER EVENTS

#### RePort Business Solutions

On November 20, 2003, the Company's Board of Directors approved entering into a revised agreement to organize a new Ontario limited partnership to acquire and operate the business of RePort Business Solutions ("RePort") in partnership with NSC Holdings Inc. ("NSCH") and Nafund Inc. ("Nafund").

This transaction was originally submitted to the stockholders of Synergx for approval at its Annual Meeting on March 26, 2003 because two directors of Synergx are directors of Nafund and one is also a director and principal

## SYNERGX SYSTEMS INC. AND SUBSIDIARIES

### NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

### 8. OTHER EVENTS (Continued)

of NSCH. Management believes that the revised structure and consideration are within the scope of the stockholder approval.

Pursuant to the revised agreement (which is subject to approval by NSCH's bank and completion of definitive documentation), the Company, through a subsidiary, would acquire from Nafund, 25% of the Class B equity units of RePort in consideration of the issuance to Nafund of 150,000 shares of Common Stock.

RePort which is currently a division of NSCH, provides software to the independent international investment counseling, portfolio management and brokerage community. Located in Toronto, Ontario, RePort's software links external or outsourced trading, custodian, broker and bank systems in internal diverse security and asset management systems and contact information systems and electronic filing and documentation systems. RePort will provide these and related back office services to NSCH (which is an investment counselor/money manager) and to other third party investment counselors, money managers, funds and similar entities.

There can be no assurance however that this transaction will take place.

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### 9. STOCK SPLIT

On July 7, 2003, the Company's Board of Directors declared a 2-for-1 stock split of its outstanding common stock. The stock split took the form of a dividend whereby the Company issued on July 25th to each shareholder of record at the close of business on July 18, 2003 one additional share for every share held on that date. The financial statements and footnotes have been retroactively adjusted to reflect this stock split.

### 10. 2004 NON-QUALIFIED STOCK OPTION PLAN

At the Company's annual meeting of stockholders on March 10, 2004 the Company and its stockholders adopted a new nonqualified stock option plan ("2004 Plan"). Under the 2004 Plan, the Board of Directors may grant options to eligible employees at exercise prices not less than 100% of the fair market value of the common shares at the time the option is granted. The number of shares of Common Stock that may be issued shall not exceed an aggregate of up to 10% of its issued and outstanding shares from time to time. Options vest at the discretion of the Board of Directors at such time as the options are granted. Issuances under the new 2004 Plan are to be reduced by options outstanding under a 1997 nonqualified stock option plan (replaced by the new 2004 Plan). Options outstanding under the 1997 Plan will expire from June 2004 through December 31, 2005. As of March 31, 2004, there were 124,914 options outstanding under the 1997 Plan and none outstanding under the 2004 Plan.

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

### Liquidity and Capital Resources

In October 2003, the Company entered into a new \$3 million revolving credit facility with Hudson United Bank. (the "Credit Facility") This credit facility has an interest rate of prime plus 1/4% and expires in October 2005. Initial proceeds from the new credit facility were used to pay off a credit facility with Citizens Business Credit. Advances under the Credit Facility are measured against a borrowing base calculated on eligible receivables and inventory. The Credit Facility is secured by all assets of the Company and all of its operating subsidiaries.

The Credit Facility includes various covenants, which among other things, impose limitations on declaring or paying dividends, acquisitions and capital expenditures. The Company is also required to maintain certain financial ratios and tangible net worth covenants. At March 31, 2004, the Company was not in default with any of its financial covenants and at such time the full amount of the Credit Facility was available under the borrowing base calculation. At March 31, 2004, \$1,846,000 was owed under the Credit Facility.

Net cash (used) by operations for the six months ended March 31, 2004 amounted to (\$763,783) as compared to cash being provided by operations of \$157,773 for the comparable prior year period. The increase in cash being used by operations was due to a (\$112,400) operating loss in the 2004 six month period compared to an operating profit of \$174,400 in the comparable 2003 period and due to an increase in working capital requirements in order to fund an increase in inventory for projects expected to be shipped after March 31, 2004. The net cash outflow of (\$763,783) from operations during 2004 coupled with equipment purchases of (\$30,004) were funded by an increase of \$590,176 in bank borrowing and from \$316,200 of proceeds from exercise of warrants to purchase common stock

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by Mirtronics and \$35,410 from exercise of stock options by employees to purchase common stock.

The ratio of the Company's current assets to current liabilities increased to approximately 2.88 to 1 at March 31, 2004 compared to 2.62 to 1 at March 31, 2003. The increase in the current ratio is due to an improvement in cash flow since March 31, 2003 due to the return to profitable operations through September 30, 2003, from \$351,610 of proceeds from the exercise of warrants and employees stock options, and from a increase of \$1.5 million of accounts receivable in 2004. Working capital increased by \$1.4 million to \$6.6 million at March 31, 2004 compared to \$5.2 million at March 31, 2003; while bank borrowing increased by \$961,000 since March 31, 2003.

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

#### Results of Operations

##### Revenues and Gross Profit

	Three Months Ended		Six Months Ended	
	March 31,		March 31,	
	2004	2003	2004	2003
	----	----	----	----
	(In thousands of dollars)			
Product Revenue	\$4,160	\$3,514	\$7,179	\$6,805
Subcontract Revenue	65	172	144	443
Service Revenue	1,165	1,103	2,269	2,178
Total Revenue	5,390	4,789	9,592	9,426
Gross Profit Product	1,345	1,242	2,261	2,270
Gross Profit Subcontract	10	27	24	87
Gross Profit Service	328	321	634	668
Total Gross Profit	1,683	1,590	2,919	3,025
Gross Profit Product %	32%	35%	31%	33%
Gross Profit Subcontract %	15%	16%	17%	20%
Gross Profit Service %	28%	29%	28%	31%

#### Revenues

The Company's product revenues during the three and six months ended March 31, 2004 increased from the comparable prior year periods, representing increases of 18% and 6% for the respective periods. These increases in product revenues resulted from an improvement in economic activity in both the Company's principal New York City market and its Dallas, Texas market. The product revenue increase during current quarter reflects strong improvement in Dallas and revenues from New York City transit projects where approvals for production and shipment were delayed last quarter and were released in the current period. However, the increase in product revenues still reflects softness in the Company's New York City market for its other products. Product revenues in our Dallas, Texas market area improved significantly from very low 2003 levels. In the Dallas, Texas market, higher product revenues resulted from certain costs

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reduction initiatives implemented during the last fifteen months, which allowed the Company to price aggressively in that competitive market. We are continuing to quote business aggressively in both that area and in the New York City metropolitan area.

Subcontract revenue decreased during the current three and six month periods as the Company was responsible for various small electrical installations during the 2004 periods which in the aggregate were less than two large electrical installation projects in 2003.

Service revenues increased during the current three and six month periods of 2004. The increase in both periods is primarily due to an increase in service contracts as the Company expanded its service base into the Long Island, NY market for fire alarm systems. In addition, the 2004 periods benefited from call-in service related to several new customers added during the current quarter.

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

#### Gross Profit

Gross profit on product revenues for the three months ended March 31, 2004, increased 8% compared to the respective prior year period. The increase in absolute gross profit is primarily related to higher product sales (noted above) and related gross margin. However, gross profit on product revenues for the six months ended March 31, 2004 decreased 1% even though products revenues increased 6% for this period. The decrease in absolute gross profit during the current six months period reflects lower profit margins resulting from aggressive pricing and from an increase in certain overhead costs. Over the last two years certain project engineers were added to support product expansion in a effort to increase products sales to a higher level. While the Company's fixed overhead cost base increased the product revenue increase did not occur by March 31, 2004. The decrease in gross profit percentage during the current three and six month periods is due to a combination of lower than anticipated sales with increased overhead, and aggressive pricing (particularly in the Dallas market area) in order to book new business.

Gross profit related to subcontract revenues for the three and six months ended March 31, 2004 decreased in absolute terms as the Company was responsible for a smaller amount of electrical installation. However, the gross profit percentage was lower during the three and six months of 2004 as markups on electrical installation were lower due to the competitive environment during this period.

Gross profit on service revenues for the three months ended March 31, 2004 increased due to the increase in service contract revenues. Gross profit from service revenues during the six months ended March 31, 2004 decreased in spite of an increase in service revenues. The gross profit decline for this period was due to an increase in technicians to support higher service revenues, salary increases, and technicians moving up to higher paying categories. These cost increases could not be fully absorbed by price increases to service contracts or by additional call-in service revenue.

#### Income Before Tax

The decline in income before income taxes during the three and six months ended

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March 31, 2004 is primarily due to the decrease in gross lower profit margins resulting from aggressive pricing in Dallas to obtain business and from an increase in certain overhead costs to support product expansion in New York in an effort to increase product sales to a higher level. This decline in income before tax was also caused by lower gross profit from subcontract revenues (three and six months of 2004) and from lower gross profit on service revenues during the six months of 2004. In addition, selling, general and administrative expenses increased (7% and 5% during the three and six months of 2004, respectively) due to higher insurance costs in 2004 and from additional management and sales staff to support product expansion directed at increased levels. Interest expense increased during 2004 due to higher borrowing levels. For the three and six month periods of 2004 the Company recorded a loss of \$12,000 and \$32,000, respectively, on its equity in the operating loss of Secure 724 LP.

### Tax Provision

The Company's current income tax provision represents federal, state and local income taxes. Deferred taxes represent the net change in deferred tax assets and non current deferred tax liability as it related to certain timing differences of book and tax deductions.

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

### Order Position

The Company's order position, excluding service, at March 31, 2004 amounted to \$15,800,000 as compared to \$16,500,000 at September 30, 2003 and \$14,100,000 at March 31, 2003. These historically high levels of order position reflects recent large new orders received for several subway complexes which will be deliverable over several years as the projects are released and reflects recent increased new orders in our Dallas, Texas Market area.. In addition, the backlog includes \$2.5 million of orders for communication and announcement systems from several transit car manufacturers, that will be shippable over the next 24 month period. While quotation activity is brisk, there is no assurance when orders will be received and whether the order position will increase. Due to the fact that the Company's products are sold and installed as part of larger mass transit construction projects, there is typically a delay between the booking of the contract and its revenue realization. The order position includes and the Company continues to bid on projects that might include significant subcontractor labor (electrical installation performed by others). The Company expects to be active in seeking orders where the Company would act as a prime contractor and be responsible for management of the project as well as electrical installation.

## Item 3. Controls and Procedures

Evaluation of disclosure controls and procedures. At the period end of this Quarterly Report on Form 10-QSB, the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded, as of the end of the quarter covered by this report, that:

The Company's disclosure controls and procedures are designed to ensure that

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information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified.

That Company's disclosure controls and procedures are effective to ensure that such information is accumulated and communicated to the Company's management, and made known to the Company's Chief Executive Officer and Chief Financial Officer, to allow timely decision regarding the required disclosure.

There have been no changes in the Company's internal controls over financial report that have materially affected, or is reasonably likely to materially affect the Company's internal controls over financial reporting during the period covered by this Quarterly Report.

### Part II - OTHER INFORMATION

#### Item 1. Legal Proceedings.

Not Applicable

#### Item 2. Changes in Securities.

Mirtronics the largest stockholder of the Company had outstanding warrants to purchase 620,000 shares of the Company's Common Stock, which were issued in 1998, and were exercisable at any time until December 31, 2003 at an exercise price of \$.51 per share. Mirtronics exercised these warrants in December 2003 for a total consideration of \$316,200.

#### Item 3. Defaults Upon Senior Securities.

Not applicable

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

The Registrant's Annual Meeting of Stockholders was held on March 10, 2004. At the meeting, Stockholders considered and voted upon:

- (1) the election of seven (7) directors to Synergx's Board of Directors,
- (2) the selection of Marcum & Kleigman LLP as Synergx's independent auditors for the fiscal year ending September 2004
- (3) to adopt the 2004 Non-Qualified Stock Option Plan.

The seven nominees for director were unopposed and were, accordingly elected by the Stockholders. The following table details the votes cast for, against and abstained from voting on each matter considered by the Stockholders.

MATTER	FOR	AGAINST
Daniel Tamkin	4,446,866	3,828
John Poserina	4,446,866	3,828
Henry Schnurbach	4,446,866	3,828
Joseph Vitale	4,446,866	3,828
Dennis McConnell	4,446,800	3,894
J Ian Dalrymple	4,446,824	3,870
Mark I. Litwin	4,446,824	3,870

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Auditors	4,444,597	2,068
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Adoption 2004 Non-Qualified Stock Option Plan	2,701,781	47,840
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Item 5. Other Information.

On January 30, 2004, the Company filed a post-effective amendment No. 1 to Form S-8 Registration Statement (Reoffer Prospectus) for 86,322 shares of Common Stock which provides for the sales thereof by certain executive officers and directors.

Item 6. Exhibits and Reports on form 8-K.

(a) Exhibits

- 31.1 Certification of Daniel S. Tamkin pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of John A. Poserina pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certifications of Daniel S. Tamkin pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certifications of John A. Poserina pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

None

Other

The information in Item 2 and Item 6 regarding shares of Common Stock have been adjusted for a 2 for 1 stock split that took the form of a dividend that was distributed on July 25, 2003.

SIGNATURES

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

SYNERGX SYSTEMS INC  
(Registrant)

/s/ JOHN A. POSERINA

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John A. Poserina,  
Chief Financial Officer  
(Principal Accounting and  
Financial Officer), Secretary  
And Director

Date: May 12, 2004



