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SYNERGX SYSTEMS INC  
Form 10QSB  
February 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 \_\_\_\_\_ December 31, 2003 \_\_\_\_\_

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  
(State or jurisdiction of incorporation (IRS employer identification Number)  
or 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 February 6, 2004, 4,706,728  
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)

|   | December 31,<br>2003 |
|---|----------------------|
|   | -----                |
| ASSETS  |                      |
| CURRENT ASSETS  |                      |
| Cash and cash equivalents   | \$ 338,805           |
| Accounts receivable, principally trade, less allowance<br>for doubtful accounts of \$415,405      | 5,300,582            |
| Inventories   | 2,672,943            |
| Deferred taxes  | 321,200              |
| Prepaid expenses and other current assets   | 318,908              |
| TOTAL CURRENT ASSETS  | 8,952,438            |
| PROPERTY AND EQUIPMENT -at cost, less<br>accumulated depreciation and amortization of \$1,401,093 | 384,960              |
| OTHER ASSETS  | 709,455              |
|   | -----                |

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TOTAL ASSETS \$10,046,853  
=====

See accompanying Notes to the Condensed Consolidated Financial Statements

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEET  
(Unaudited)

December 31,  
2003  
-----

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES

|  |           |
|--|-----------|
| Notes and capital leases payable - current portion | \$ 47,150 |
| Accounts payable and accrued expenses              | 2,336,680 |
| Deferred revenue                                   | 377,391   |

|                           |                    |
|---------------------------|--------------------|
| TOTAL CURRENT LIABILITIES | -----<br>2,761,221 |
|---------------------------|--------------------|

|   |           |
|---|-----------|
| Note payable to bank                                    | 1,560,676 |
| Notes and capital leases payable - less current portion | 40,657    |
| Deferred taxes  | 17,900    |

|                   |                             |
|-------------------|-----------------------------|
| TOTAL LIABILITIES | -----<br>4,380,454<br>----- |
|-------------------|-----------------------------|

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY

|  |           |
|--|-----------|
| Preferred stock, 2,000,000 shares authorized-<br>none issued and outstanding                             |           |
| Common stock, 10,000,000 shares authorized, \$.001<br>par value; issued and outstanding 4,687,394 shares | 4,687     |
| Capital in excess of par   | 6,296,600 |
| Accumulated deficit  | (634,888) |

|                            |                             |
|----------------------------|-----------------------------|
| TOTAL STOCKHOLDERS' EQUITY | -----<br>5,666,399<br>----- |
|----------------------------|-----------------------------|

|  |                       |
|--|-----------------------|
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$10,046,853<br>===== |
|--|-----------------------|

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 December 31,<br>2003 | 2002         |
|---|---|--------------|
|   | -----   | -----        |
| Product sales   | \$ 3,018,948                                    | \$ 3,291,305 |
| Subcontract sales   | 78,935  | 270,899      |
| Service revenue   | 1,103,923                                       | 1,075,315    |
|   | -----   | -----        |
| Total revenues  | 4,201,806                                       | 4,637,519    |
|   | -----   | -----        |
| Cost of product sales   | 2,102,751                                       | 2,263,483    |
| Cost of subcontract sales   | 65,515  | 210,514      |
| Cost of service   | 797,282   | 727,761      |
| Selling, general and administrative   | 1,362,741                                       | 1,329,143    |
| Interest expense  | 19,370  | 10,118       |
| Depreciation and amortization   | 48,443  | 44,678       |
| Loss on equity investment   | 20,000  |              |
|   | -----   | -----        |
|   | 4,416,102                                       | 4,585,697    |
|   | -----   | -----        |
| (Loss) Income before (benefit) provision for<br>income taxes                | (214,296)                                       | 51,822       |
|   | -----   | -----        |
| (Benefit) provision for income taxes:                                       |   |              |
| Current   | (62,200)  | 24,000       |
| Deferred  | (25,800)  | 6,000        |
|   | -----   | -----        |
|   | (88,000)  | 30,000       |
|   | -----   | -----        |
| Net (Loss) Income   | (126,296)                                       | \$ 21,822    |
|   | =====   | =====        |
| (Loss) earnings per common share  |   |              |
| Basic (loss) earnings per share   | \$ (0.03)                                       | \$ 0.01      |
|   | =====   | =====        |
| Diluted (loss) earnings per share   | \$ (0.03)                                       | \$ 0.01      |
|   | =====   | =====        |
| Weighted average number of common shares outstanding                        | 4,166,103                                       | 3,748,850    |
| Weighted average number of common and dilutive<br>common shares outstanding | 4,166,103                                       | 3,930,489    |

See accompanying Notes to the Condensed Consolidated Financial Statements

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

For the Three Months Ended Dec  
2003 2002

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|  |              |           |
|--|--------------|-----------|
| OPERATING ACTIVITIES   |              |           |
| Net (loss) income  | \$ (126,296) | \$ 21,82  |
| Adjustments to reconcile net (loss) income to net cash used in operating activities: |              |           |
| Depreciation and amortization  | 48,443       | 44,67     |
| Deferred (benefit) tax   | (25,800)     | 6,00      |
| Provision for doubtful accounts  | 4,000        | (14,70    |
| Loss on equity investment  | 20,000       |           |
| Changes in operating assets and liabilities:   |              |           |
| Accounts receivable  | 489,339      | (513,32   |
| Inventories  | (224,373)    | (510,07   |
| Prepaid expenses and other current assets  | (2,712)      | (7,27     |
| Other assets   | (35,752)     | (52,25    |
| Accounts payable and accrued expenses  | (589,584)    | 945,55    |
| Deferred revenue   | (57,500)     | 13,42     |
| NET CASH USED IN OPERATING ACTIVITIES  | (500,235)    | (66,16    |
| INVESTING ACTIVITIES   |              |           |
| Purchases of property and equipment  | (9,321)      | (58,22    |
| NET CASH USED IN INVESTING ACTIVITIES  | (9,321)      | (58,22    |
| FINANCING ACTIVITIES   |              |           |
| Principal payments on notes payable and capital lease obligations                    | (69,326)     | (39,47    |
| Payments and proceeds from revolving line of credit - net                            | 305,176      | 178,65    |
| Proceeds from exercise of stock options and warrants                                 | 319,325      |           |
| NET CASH PROVIDED BY FINANCING ACTIVITIES  | 555,175      | 139,17    |
| NET INCREASE IN CASH AND CASH EQUIVALENTS  | 45,619       | 14,78     |
| Cash and cash equivalents at beginning of period                                     | 293,186      | 200,20    |
| Cash and cash equivalents at end of period   | \$ 338,805   | \$ 214,99 |
| SUPPLEMENTAL CASH FLOW INFORMATION:  |              |           |
| Cash paid during the period for:   |              |           |
| Income taxes   | \$ 130,519   | \$ 4,70   |
| Interest   | \$ 27,200    | \$ 12,14  |

SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:

During the quarter ended December 31, 2003 and 2002, 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

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THREE MONTHS ENDED DECEMBER 31, 2003

(UNAUDITED)

## 1. BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in accordance 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 months ended December 31, 2003 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 December 31, 2003 and 2002 and have been included in accounts receivable. There were no billing in excess of costs and estimated profits at December 31, 2003 and 2002.

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

THREE MONTHS ENDED DECEMBER 31, 2003

(UNAUDITED)

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### 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

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 (4.5% at December 31, 2003) 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 December 31, 2003 the full amount of the Credit Facility was available under the borrowing base calculation and \$1,561,000 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 December 31, 2003 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 three months ending December 31, 2003, employee stock options to purchase 6,250 shares of Common Stock were exercised for a total consideration of \$3,125.

## SYNERGX SYSTEMS INC. AND SUBSIDIARIES

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

THREE MONTHS ENDED DECEMBER 31, 2003

(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 options, non-employee stock options and warrants. The Company did not have stock based compensation for the three months ended December 31, 2003 or 2002

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| Basic EPS Computation   | For the Three Months ended December 31, |           |
|---|---|-----------|
|   | 2003                                    | 2002      |
|   | -----                                   | -----     |
| Net (Loss) Income available to common stockholders                        | \$ (126,296)                            | \$ 21,822 |
| Weighted average outstanding shares                                       | 4,166,103                               | 3,748,850 |
| Basic (Loss) EPS  | \$ (.03)                                | \$ .01    |
|   | =====                                   | =====     |
| Diluted EPS Computation   |   |           |
| (Loss) Income available to common stockholders<br>and assumed conversions | \$ (126,296)                            | \$ 21,821 |
|   | -----                                   | -----     |
| Weighted-average shares   | 4,166,103                               | 3,748,850 |
|   | -----                                   | -----     |
| Plus: Incremental shares from assumed conversions                         |   |           |
| Employee Stock Options*   |   | 40,730    |
| Warrants*   |   | 140,909   |
|   |   | -----     |
| Dilutive potential common shares  | N/A                                     | 181,639   |
|   | -----                                   | -----     |
| Adjusted weighted-average shares  | 4,166,103                               | 3,930,489 |
|   | =====                                   | =====     |
| Diluted (Loss) EPS  | \$ (.03)                                | \$ .01    |
|   | =====                                   | =====     |

\*All warrants and options were antidilutive in 2003 and 340,000 warrants were antidilutive for 2002 and therefore not included in the above calculations.

SYNERGX SYSTEMS INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

THREE MONTHS ENDED DECEMBER 31, 2003

(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 \$225,000 U.S. at December 31, 2003) 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



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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 month ended December 31, 2003, a \$20,000 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

THREE MONTHS ENDED DECEMBER 31, 2003

(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

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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.

### 9. STOCK SPLIT

On July 7, 2003, the Company's Board of Directors declared a 2-for-1 stock split of its outstanding 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 adjusted to reflect this stock split.

## 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 December 31, 2003, 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 December 31, 2003, \$1,561,000 was owed under the Credit Facility.

Net cash (used) by operations for the three months ended December 31, 2003 amounted to \$(500,235) as compared to (\$66,167) for the comparable prior year period. The increase in cash being used by operations was due to a (\$214,000) operating loss in the 2003 quarter compared to an operating profit of \$52,000 in the comparable 2002 period and due to an increase in working capital requirements in order to pay down accounts payable and accrued expenses by \$100,245 in excess of accounts receivable collections and for an increase in inventory for projects expected to be shipped after December 31, 2003. The net cash outflow of \$(500,235) from operations during 2003 coupled with equipment purchases of (\$9,321) were funded by an increase of \$305,176 in bank borrowing and from \$316,200 of proceeds from exercise of warrants to purchase common stock by Mirtronics and \$3,125 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 3.20 to 1 at December 31, 2003 compared to 2.19 to 1 at December 31, 2002. The increase in the current ratio is due to an improvement in cash flow since December 31, 2002 due to the return to profitable operations through September 30, 2003, from \$319,325 of proceeds from the exercise of warrants and employees stock options, and from a major reduction in 2003 of accounts payable and accrued expenses from higher collections of accounts receivable in 2003.

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Working capital increased to a high level of \$6.2 million at December 31, 2003 compared to \$5.3 million at December 31, 2002; while bank borrowing increased by \$544,000 since December 31, 2002.

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

#### Results of Operations

##### Revenues and Gross Profit

|                            | Three Months Ended<br>December 31, |         |
|----------------------------|------------------------------------|---------|
|                            | 2003                               | 2002    |
|                            | (In thousands of dollars)          |         |
| Product Revenue            | \$3,019                            | \$3,292 |
| Subcontract Revenue        | 79                                 | 271     |
| Service Revenue            | 1,104                              | 1,075   |
|                            | -----                              | -----   |
| Total Revenue              | \$4,202                            | \$4,638 |
| <br>                       |                                    |         |
| Gross Profit Product       | \$ 916                             | \$1,028 |
| Gross Profit Subcontract   | 13                                 | 60      |
| Gross Profit Service       | 307                                | 348     |
|                            | -----                              | -----   |
| Total Gross Profit         | \$1,236                            | \$1,436 |
| <br>                       |                                    |         |
| Gross Profit Product %     | 30%                                | 31%     |
| Gross Profit Subcontract % | 16%                                | 22%     |
| Gross Profit Service %     | 28%                                | 32%     |
|                            | -----                              | -----   |
| Total Gross Profit %       | 29%                                | 31%     |

#### Revenues

The Company's product revenues during the three months ended December 31, 2003 were \$3,019,000 compared to \$3,292,000 for the prior year period. This decrease of 8% was caused in part by certain revenues from New York City Transit projects where approvals for production and shipment were received late in the quarter and accordingly production was delayed. The decrease in product revenues also reflects softness in the Company's principal New York City market for its other products. However, product revenues in our Dallas, Texas market area improved significantly from the very low 2002 level. In the Dallas, Texas market, higher product revenues resulted from certain cost reduction initiatives implemented during the last twelve months which allowed the Company to price aggressively in that competitive market. We continue to quote business aggressively in both that area and in New York City Metropolitan area. As a consequence, new order bookings improved for the three months ended December 31, 2003 and new orders remain at a near record level.

Subcontract revenue decreased during the current three month period to \$79,000 from \$271,000 in the comparable prior year period. The Company was responsible for various small electrical installations during the 2003 period as compared to two large electrical installation projects in 2002.

Service revenues increased during the current three month period primarily due

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to an increase in service contracts as the Company expanded its service base into the Long Island, New York market area for fire alarm systems.

### 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 December 31, 2003, decreased 11% to \$916,000 compared to \$1,028,000 for the prior year period. The decrease in absolute gross profit is primarily related to lower product sales (noted above) and related gross margin. The decrease in gross profit percentage in 2003 to 30% compared to 31% in 2002 reflects lower sales in which to absorb certain fixed overhead costs. Over the last two years, certain project engineers were added to support product expansion in an effort to increase product sales to a higher level. While the Company's fixed overhead cost base increased the product revenue increase did not occur by December 31, 2003. A combination of lower sales and increased overhead contributed to a lower gross margin percentage.

Gross profit related to subcontract revenues for the three months ended December 31, 2003 decreased in absolute terms as the Company was responsible for a smaller amount of electrical installation. In addition, the gross profit percentage was lower during the three months of 2003 as mark ups on electrical installations were lower due to the competitive environment during this period.

Gross profit from service revenues during the three months ended December 31, 2003 decreased in spite of the increase in service revenue. The gross profit decline was due from an increase in technicians to support higher service revenue, salary increases and technicians moving up to higher paying categories. These cost increases could not be fully absorbed by price increases to service contracts.

#### Income Before Tax

The decline in income before income taxes during the three months ended December 31, 2003 is primarily due to the decrease in gross profit caused by lower product revenues and related gross margin and from the relative fixed nature of certain overhead costs (noted above). This decline in income before tax was also caused by lower gross profit from subcontract revenues and from service revenues. In addition, selling, general and administrative expenses increased (3%) to support higher product sales and from higher insurance costs during 2003. Interest expense increased during 2003 due to higher borrowing levels. For 2003, the Company also recorded a loss of \$20,000 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.

#### Order Position

The Company's order position, excluding service, at December 31, 2003 was \$16,150,000 as compared to \$16,500,000 at September 30, 2003 and \$12,620,000 at December 31, 2002. This near record order position, reflects recent large new orders received for several subway complexes which will be deliverable over

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several years as the projects are released and reflects recent increased new orders in our Dallas, Texas market area.

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

In addition, the backlog includes \$1.8 million of orders for communication and announcement systems from several transit car manufacturers, that will be shippable over the next 15 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 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

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### 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.

Not applicable

### Item 5. Other Information.

Subsequent to December 31, 2003, 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)

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/s/ John A. Poserina

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

Date: February 12, 2004