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DIVERSIFIED SECURITY SOLUTIONS INC  
Form 10QSB  
August 13, 2004

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-QSB

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

For the quarterly period ended June 30, 2004

OR

TRANSITION REPORT UNDER SECTION 13 OR 15 (D) OF THE SECURITIES AND EXCHANGE  
ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File No. 05-62411

Diversified Security Solutions, Inc.  
(Name of small business issuer as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

22-3690168  
(I.R.S. Employer  
Identification No.)

280 Midland Avenue  
Saddle Brook, New Jersey 07663  
(address of principal executive offices) (Zip Code)

Issuer's Telephone number, including area code: (201) 794-6500

Check whether Issuer (1) filed all reports required to be filed by Section 13 or 15 (d) of the Exchange Act during the past 12 months (or for such shorter period that the issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Number of shares outstanding of the issuer's Common Stock:

| Class:                        | Outstanding as of August 13, 2004, |
|-------------------------------|------------------------------------|
| -----                         | -----                              |
| Common stock, \$.01 par value | 5,740,398                          |

Diversified Security Solutions, Inc. and Subsidiaries

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Item 1. Financial Statements

DIVERSIFIED SECURITY SOLUTIONS, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

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June 30, 2004  
(Unaudited)

|   | June 30, 2004<br>(Unaudited) |
|---|------------------------------|
| ASSETS  |                              |
| CURRENT ASSETS:   |                              |
| CASH AND CASH EQUIVALENT  | \$ 1,571,691                 |
| ACCOUNTS RECEIVABLE - NET OF ALLOWANCES OF \$225,000 AND \$135,000  | 7,496,008                    |
| INVENTORIES   | 1,214,524                    |
| COSTS IN EXCESS OF BILLINGS AND ESTIMATED PROFITS   | 950,237                      |
| DEFERRED TAX ASSETS   | 2,310,375                    |
| PREPAID AND INCOME TAXES RECEIVABLE   | 324,434                      |
| OTHER ASSETS  | 243,942                      |
|   | -----                        |
| TOTAL CURRENT ASSETS  | 14,111,211                   |
| PROPERTY AND EQUIPMENT - net of accumulated depreciation of \$1,418,962<br>and \$1,406,824                | 1,146,943                    |
| GOODWILL  | 2,221,955                    |
| INTANGIBLE ASSETS - net of accumulated amortization of \$241,741 and \$179,809                            | 1,233,547                    |
| OTHER ASSETS  | 641,635                      |
|   | -----                        |
| TOTAL CURRENT ASSETS  | \$19,355,290<br>=====        |
| LIABILITIES & STOCKHOLDERS' EQUITY  |                              |
| CURRENT LIABILITIES:  |                              |
| ACCOUNTS PAYABLE  | \$ 2,862,195                 |
| ACCRUED TAXES & EXPENSES  | 1,019,626                    |
| BILLING IN EXCESS OF COST AND ESTIMATED PROFITS   | 1,380,495                    |
| DEFERRED INCOME   | 151,566                      |
| LONG-TERM DEBT, CURRENT PORTION   | 2,033,158                    |
| CUSTOMER DEPOSITS   | 77,863                       |
| DEFERRED TAX LIABILITY  | 64,000                       |
|   | -----                        |
| TOTAL CURRENT   | 7,588,903                    |
| LONG-TERM DEBT, LESS CURRENT PORTION  | 160,295                      |
| DEFERRED TAX LIABILITY  | 134,000                      |
|   | -----                        |
| TOTAL LONG-TERM LIABILITIES   | 7,883,198<br>-----           |
| STOCK HOLDERS' EQUITY:  |                              |
| PERFERRED STOCK, \$.01PAR VALUE: 2,000,000 SHARES AUTHORIZED;<br>NO SHARES ISSUED                         | --                           |
| COMMON STOCK, \$.01PAR VALUE: 10,000,000 SHARES AUTHORIZED;<br>5,248,531 and 5,201,431 SHARES OUTSTANDING | 52,485                       |
| ADDITIONAL PAID-IN-CAPITAL  | 14,062,565                   |
| TREASURY STOCK, AT COST 70,891 SHARES   | (500,000)                    |
| DEFERRED COMPENSATION   | (201,191)                    |
| ACCUMULATED DEFICIT   | (1,941,767)                  |
|   | -----                        |
| TOTAL STOCKHOLDERS' EQUITY  | 11,472,092<br>-----          |
| TOTAL LIABILITIES and STOCKHOLDERS' EQUITY  | \$19,355,290<br>=====        |

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The accompanying notes are an intergral part of these financial statements.

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## DIVERSIFIED SECURITY SOLUTIONS, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

|  | Six Months Ended |                | Three Months Ended |               |
|--|------------------|----------------|--------------------|---------------|
|  | JUNE 30, 2004    | JUNE 30, 2003  | JUNE 30, 2004      | JUNE 30, 2003 |
| Sales                                      | \$12,191,983     | \$ 7,226,421   | \$ 6,524,490       | \$ 3,811,421  |
| Cost of Sales                              | 9,384,475        | 5,604,699      | 4,995,689          | 2,811,421     |
| Gross Profit                               | 2,807,508        | 1,621,722      | 1,528,801          | 1,000,000     |
| Operating Expenses:                        |                  |                |                    |               |
| Selling General & Administrative Expenses  | 3,026,223        | 4,385,578      | 1,599,389          | 2,000,000     |
| Operating Loss                             | (218,715)        | (2,763,856)    | (70,588)           | (1,000,000)   |
| Interest Income                            | 3,404            | 6,733          | 1,879              | 6,733         |
| Interest Expense                           | (49,019)         | (51,114)       | (24,211)           | (51,114)      |
| Net (Loss) Before Tax Benefit              | (264,330)        | (2,808,237)    | (92,920)           | (1,000,000)   |
| Tax Benefit For Income Tax                 | 108,375          | 1,179,000      | 38,097             | 1,179,000     |
| Net (Loss) After Tax Benefit               | \$ (155,955)     | \$ (1,629,237) | \$ (54,823)        | \$ 179,000    |
| Basic and Diluted (Loss) Per Common Share: |                  |                |                    |               |
| Basic (Loss) Per Common Share              | \$ (0.03)        | \$ (0.32)      | \$ (0.01)          | \$ 0.18       |
| Weighted Average Common Shares             | 5,143,908        | 5,138,357      | 5,157,129          | 1,000,000     |
| Diluted (Loss) Per Common Share:           | \$ (0.03)        | \$ (0.32)      | \$ (0.01)          | \$ 0.18       |
| Weighted Average Diluted Common Shares     | 5,143,908        | 5,138,357      | 5,157,129          | 1,000,000     |

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

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DIVERSIFIED SECURITY SOLUTION, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

|   | For The Six Months |         |
|---|--------------------|---------|
|   | June 2004          | June    |
|   | -----              | -----   |
| Cash flows from operating activities:                             |                    |         |
| Net loss  | \$ (155,955)       | \$ (1,6 |
| Adjustments to reconcile net loss from operations                 |                    |         |
| to net cash provide by (used in) operating activities:            |                    |         |
| Depreciation and amortization                                     | 259,672            | 2       |
| Bad debt expense  | 90,000             |         |
| Stock option expense  | 18,707             |         |
| Deferred income taxes   | (108,375)          | (3      |
| Changes in operating assets and liabilities:                      |                    |         |
| Accounts receivable   | (873,015)          | 9       |
| Inventories   | (125,285)          | 3       |
| Costs and estimated profits in excess of billings                 | (184,332)          | 5       |
| Other assets  | (214,620)          | 2       |
| Prepaid and income taxes receivable                               | (138,807)          | (1,0    |
| Accounts payable  | 646,494            | (2      |
| Accrued expenses  | 49,362             | (       |
| Billings in excess of cost and estimated profits                  | 902,980            | 1       |
| Deferred income   | (3,711)            |         |
| Customer deposits held  | 53,438             | (1      |
|   | -----              | -----   |
| Net cash provided by (used in) operating activities               | \$ 216,552         | \$ (9   |
|   | -----              | -----   |
| Cash flows from investing activities:                             |                    |         |
| Proceeds from issuance of common stock                            | 63,799             |         |
| Purchase of business, net of cash acquired                        | (166,875)          |         |
| Purchase of property and equipment                                | (49,053)           | (1      |
| Increase in Goodwill for guarantee of stock price                 | --                 | (       |
|   | -----              | -----   |
| Cash used in investing activities                                 | \$ (152,129)       | \$ (2   |
|   | -----              | -----   |
| Cash flows from financing activities:                             |                    |         |
| Net (payments) and proceeds of revolving bank line and other debt | (320,148)          | 3       |
| Payment of loan payable to owner of acquired company              | (100,000)          |         |
|   | -----              | -----   |
| Cash (used in) proceeds financing activities                      | \$ (420,148)       | \$ 3    |
|   | -----              | -----   |
| Decrease in cash and cash equivalents                             | (355,725)          | (9      |
| Cash and cash equivalents - beginning of period                   | 1,927,416          | 4,4     |
|   | -----              | -----   |
| Cash and cash equivalents - end of period                         | \$1,571,691        | \$ 3,5  |
|   | -----              | -----   |
| Supplemental disclosure of cash flow information:                 |                    |         |
| Amount paid for the period for:                                   |                    |         |
| Interest  | \$ 49,562          | \$      |
| Taxes   | \$ 1,600           | \$ 1    |
| Non-cash investing and financing activities:                      |                    |         |
| Equipment financed  | \$ 127,371         | \$      |
| Stock issued to acquire business                                  | \$ 266,400         | \$      |

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Value of stock options issued

\$ 219,898 \$

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

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## DIVERSIFIED SECURITY SOLUTIONS, INC AND SUBSIDIARIES NOTES TO FINANCIAL STATEMENTS

### 1. Basis of Presentation

Diversified Security Solutions, Inc., the ("Company") and its subsidiaries, are systems integrators providing design, installation and support services for a wide variety of security, communications and control systems. The Company specializes in turnkey systems that integrate many different technologies. Systems are customized to meet the specific needs of its customers. The Company markets nationwide with an emphasis in the New York City, Dallas, Phoenix and Southern California metropolitan areas. Customers are primarily medium and large businesses and governmental agencies. The Company derives a majority of its sales from project installations and to a smaller extent, service sales (maintenance). In April of 2004, the Company completed its acquisition of Airorlite Communication's, Inc. ("Airorlite"). Airorlite specializes in the design, manufacturing and maintaining wireless communications equipment used to enhance and extend emergency radio frequency services and cellular communication for both fixed and mobile applications. There has been a shift in sales by geographic region and therefore, the information below shows the sales percentages by geographic location for the six months ended June 30, 2004 and 2003 as follows:

|                      | Six Months<br>Ended June 30, |      |
|----------------------|------------------------------|------|
|                      | 2004                         | 2003 |
|                      | ----                         | ---- |
| New Jersey/ New York | 38%                          | 52%  |
| California           | 35                           | 26   |
| Texas                | 14                           | 13   |
| Arizona              | 7                            | 5    |
|                      | ---                          | ---  |
| Total integration    | 94                           | 96   |
| Airorlite            | 4                            | 0    |
| Viscom               | 2                            | 4    |
|                      | ---                          | ---  |
| Total sales          | 100%                         | 100% |
|                      | ===                          | ===  |

The Company's headquarters are located in Saddle Brook, New Jersey. Sales and service facilities are located near the Dallas Fort Worth Airport, Phoenix

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Arizona Airport, two facilities in the New York City metro area ( Saddle Brook, New Jersey), and Fullerton, California. During the third quarter of 2003, the Company's subsidiary, Viscom Products ("Viscom"), restructured its operations to begin outsourcing the manufacturing of its products to a third party. Viscom will continue to sell product and support existing warranties.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles in the United States for full year financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal, recurring nature. Operating results for the three month and six month period ended June 30, 2004, are not necessarily indicative of the results that may be expected for the year ended December 31, 2004. These consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto that are included in the Company's Annual Report on Form 10-KSB for the fiscal period ended December 31, 2003.

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### DIVERSIFIED SECURITY SOLUTIONS, INC AND SUBSIDIARIES NOTES TO FINANCIAL STATEMENTS

#### 2. Net Income (Loss) Per Share

The computation of basic earnings (loss) per share is based upon the weighted average number of shares of common stock outstanding during the period. The computation of diluted earnings per share includes the dilutive effects of common stock equivalents of options and warrants.

#### 3. Stock Based Compensation

In December 2002, the FASB issued SFAS No. 148 "Accounting for Stock Based Compensation- Transition and Disclosure". SFAS No. 148 provides alternative methods of transitions to SFAS No 123's fair value method of accounting for stock based employee compensation, but does not require companies to use fair value method. It also amends the disclosure provisions of SFAS No. 123 and APB No.25 to require, in the summary of significant policies, the effect of an entity's accounting policy with respect to stock based employee compensation on reported net income and earnings per share in annual and interim financial statements. The provision of this statement is effective for fiscal years ending after December 15, 2002, and interim reporting periods beginning after December 15, 2002. Accordingly, the fair value of all options granted on and after January 1, 2003 is to be charged against income over the vesting period. For the six months ended June 30, 2004, the Company charged \$18,707 of options granted subsequent to January 1, 2003 against 2004 earnings. Those issued prior to adoption are accounted for under the intrinsic value method in accordance with APB No. 25. The Company adopted the perspective method as permitted by SFAS No. 148 on January 1, 2003.

Based upon the fair value method to measure compensation expense, the Company's proforma effects for the three and six months ended June 30, 2004 and 2003 is as follows:

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|  | Six Monthd Ended<br>June 30<br>(Unaudited) |               | Three Monthd Ended<br>June 30<br>(Unaudited) |             |
|--|--|---------------|--|-------------|
|  | 2004                                       | 2003          | 2004   | 2003        |
| Net loss per Financial Statements  | (\$155,955)                                | (\$1,629,237) | (\$54,823)                                   | (\$966,081) |
| Stock based-employee compensation<br>expense included in reported net loss,<br>net of related tax expense            | 7,670                                      | --            | 7,670  | --          |
| Total stock-based employee compensation<br>expense determined under fair valued based,<br>net of related tax effects | (11,216)                                   | (8,489)       | (7,797)                                      | (4,404)     |
| Pro forma net loss   | (\$159,501)                                | (\$1,637,726) | (\$54,950)                                   | (\$970,485) |
| Loss per share:  |  |               |  |             |
| Basis and diluted shares as reported   | (\$0.03)                                   | (\$0.32)      | (\$0.01)                                     | (\$0.19)    |
| Basis and diluted shares as proforma   | (\$0.03)                                   | (\$0.32)      | (\$0.01)                                     | (\$0.19)    |

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DIVERSIFIED SECURITY SOLUTIONS, INC AND SUBSIDIARIES  
NOTES TO FINANCIAL STATEMENTS

4. Related Party Transaction

A corporation of which a director of the Company was an officer was paid consulting fees and reimbursement of expenses in amount of approximately \$15,877 for the six months ended June 30,2004 and \$30,900 for the six months ended June 30, 2003.

5. Acquisition

Effective April 1, 2004, ACI Acquisition Corporation, a wholly-owned subsidiary of the Company, purchased all of the issued and outstanding stock of Airorlite Communications, Inc ("Airorlite"). Airorlite was purchased for \$200,000 cash, 37,000 shares of the Company's common stock, valued at \$266,400, concurrently with the closing, an officer's loan of \$100,000 was repaid and an amount equal to the income tax on the undistributed earnings for the period January 1, 2004 to the acquisition of the Company. Airorlite is located in Saddle Brook, New Jersey and specializes in design, manufacturing and



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maintaining wireless communications equipment used to enhance and extend emergency radio frequency services and cellular communication for both fixed and mobile applications. Airorlite has been merged into ACI and ACI has been renamed Airorlite Communications, Inc. The Company accounted for the acquisition under the purchase accounting method. Accordingly, assets and liabilities were recorded at their fair value. As a result of the acquisition, the Company recorded goodwill of \$291,260. The following summarized the net assets acquired from Airorlite Communications (prior to acquisition accounting adjustments) as of April 1, 2004:

|                     | Balance   |
|---------------------|-----------|
|                     | -----     |
| Current assets      | \$410,829 |
| Long term assets    | 16,003    |
| Current liabilities | 208,970   |
|                     | -----     |
| Net assets          | \$217,862 |
|                     | =====     |

Airorlite Communications had sales of \$523,386 (unaudited) for the three months ended June 30, 2004 with an operating profit of approximately \$183,556. The unaudited net assets (excluding goodwill) as of June 30, 2004 were \$558,696.

### 6. Subsequent Event

On July 28 2004 the Company completed a \$3,300,000 private placement of its common stock to certain qualified institutional investors. Under the terms of the agreement, the Company sold 553,333 shares of common stock to qualified investors for \$6.00 per share. The Company also has granted the investors a warrant to acquire 138,333 shares of common stock at an exercise price of \$7.60 per share, exercisable for a period commencing six months after the date of issuance through the fifth anniversary of the issuance. In addition, the Placement Agent received a commission of 8% of the proceeds plus expenses and was issued a warrant to acquire 55,333 shares of common stock with the same terms as those issued to the institutional investors. After expenses, the net proceeds of the transaction were approximately \$3,000,000. The Company intends to use the net proceeds of the private placement for general corporate purposes.

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## DIVERSIFIED SECURITY SOLUTIONS, INC AND SUBSIDIARIES NOTES TO FINANCIAL STATEMENTS

### 7. Contingent Liabilities

From time to time, the Company is subject to various claims with respect to matters arising out of the normal course of business. In management's opinion, none of these claims is likely to have a material affect on the Company's financial statements.

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### Critical Accounting Policies

Disclosure of the Company's significant accounting policies is included in Note 1 to the consolidated financial statements of the Company's Annual Report on Form 10-KSB for the year ended December 31, 2003. Some of these policies require management to make estimates and assumptions that may affect the reported amounts in the Company's financial statement.

### Forward Looking Statements

When used in this discussion, the words "believes", "anticipates", "contemplated", "expects", or similar expressions are intended to identify forward looking statements. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected. Those risks and uncertainties include changes in interest rates, the ability to control costs and expenses, significant variations in recognized revenue due to customer caused delays in installations, cancellations of contracts by our customers, and general economic conditions which could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company undertakes no obligation to publicly release the results of any revisions to those forward looking statements that may be made to reflect events or circumstances after this date or to reflect the occurrence of unanticipated events.

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

### Results of Operations

#### Six Months Ended June 30, 2004 and June 30, 2003

Sales - Sales for the six months ended June 30, 2004 were \$12,191,983 representing an increase of \$4,965,562 or 69% as compared to \$7,226,421 for the six months ended June 30, 2003. This sales increase is believed to be due to improved general economic conditions and an enhanced emphasis on security. The Airorlite acquisition accounted for an increase in the Company's sales of \$523,386. Each of the Company's four regions experienced significant sales growth during the six months ended June 30, 2004 as compared to the June 30, 2003 period. The Company backlog as of June 30, 2004 is \$22,500,000, representing a historical high for the Company.

Cost of Sales - Cost of sales for the six months ended June 30, 2004 was \$9,384,475 as compared to \$5,604,699 for the six months ended June 30, 2003. The gross profit margin for the six months ended June 30, 2004 was 23.0% as compared to 22.4% for the six months ended June 30, 2003. The improved gross profit percentage is due to higher margins reported in Arizona and New Jersey and the addition of the higher margin Airorlite sales. This was partially offset by decreased margins in California due to higher labor costs to complete projects on the West coast.

Selling, General and Administrative Expenses - Selling, general and administrative expenses was \$3,026,223 for the six months ended June 30, 2004 as

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compared to \$4,385,578 for the six months ended June 30, 2003. This decrease of 31.0% or \$1,359,355 was primarily attributed to savings from employee reductions, salary reductions for key employees, employee benefit reductions (health insurance, 401k, etc) and the implementation of other general cost reductions during the six months of 2004.

Interest Income - Interest income for the six months ended June 30, 2004 was \$3,404 as compared to \$6,733 for six months ended June 30, 2003. This decrease of \$3,329 was due to having less cash to invest and lower interest rates.

Interest Expense - Interest expense for the six months ended June 30, 2004 was \$49,019 as compared to \$51,114 for the six months ended June 30, 2003. The decrease of \$2,095 and is due to having a lower average debt balance for the six months ended June 30, 2004 of \$2,076,333 versus \$2,325,650 for the three months ended June 30, 2003.

### Three Months Ended June 30, 2004 and June 30, 2003

Sales - Sales for the three months ended June 30, 2004 were \$6,524,490 representing an increase of \$3,003,772 or 85.3% as compared to \$3,520,718 for the three months ended June 30, 2003. The Airorlite acquisition accounted for an increase in sales of \$523,386. Each of the Company's four regions experienced significant sales growth during the three months ended June 30, 2004 as compared to the June 30, 2003 period due to would what is believed to be improving economic conditions and increased emphasis on security.

Cost of Sales - Cost of sales for the three months ended June 30, 2004 was \$4,995,689 as compared to \$2,950,163 for the three months ended June 30, 2003. The gross profit margin for the three months ended June 30, 2004 was 23.4% as compared to 16.2% for the three months ended June 30, 2003. We attribute this 7.2% increase in the gross profit margin to improved cost control

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in all of the Company's regions and the addition of the Airorlite sales, which have a higher gross profit percentage.

Selling, General and Administrative Expenses - Selling, general and administrative expenses was \$1,599,389 for the three months ended June 30, 2004 as compared to \$2,212,438 for the three months ended June 30, 2003. This decrease of 27.7% or \$613,049 was primarily attributed to savings from head count reductions, salary reductions for key employees, selective payroll reductions (health insurance, 401k, etc) and the implementation of other general cost reductions for the three months ended June 2004.

Interest Income - Interest income for the three months ended June 30, 2004 was \$1,879 as compared to \$1,193 for three months ended June 30, 2003. This was an increase of \$686.

Interest Expense - Interest expense for the three months ended June 30, 2004 was \$24,211 as compared to \$24,391 for the three months ended June 30, 2003. The average debt balance for the three Months ended June 30, 2004 was \$2,192,489 as compared to \$2,222,355 for the three months ended June 30, 2003.

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Liquidity and Capital Resources - As of June 30, 2004, we had cash and cash equivalents \$1,571,691. We have a loan facility of \$4,500,000 with Hudson United Bank ("HUB") and have certain debt maturing from November 2004 through May 2005. The Company's outstanding loan balance with Hudson United Bank was \$2,042,628 (\$1,975,215 was current portion) and approximately \$2,186,575 was available under HUB credit facility as of June 30, 2004. Our working capital was \$6,522,308 as of June 30, 2004. The Company was in violation of various loan covenants within its debt agreement with HUB as of June 30, 2004. HUB waived these covenants.

During the six months ended June 30, 2004, net cash provided by operating activities was \$216,552. We purchased property and equipment of \$49,053. In addition, due to positive cash flows from operations, the Company was to pay HUB more than the required minimum payments of its credit facility of \$320,148. The total debt service payments were \$49,562 for the six months ended June 30, 2004.

Our working capital requirements have grown and as a result, our cash and cash equivalents have significantly decreased over the last few years. On July 28, 2004, the Company completed a \$3,300,000 private placement of its common stock to certain qualified institutional investors, which netted the Company approximately \$3,000,000 after expenses. (See Note 6 for additional details). We believe that our current cash and available lines of credit should be sufficient to meet our capital requirements for the next twelve months. However, we may seek additional equity and or debt financing as our operations continue to grow.

### Item 3. Controls and Procedures

The Company's executive management, including the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, conducted an evaluation as of the end of the period covered by this report, of the effectiveness of the Company's disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based on that evaluation, the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report. As required by Rule 13a-15(d), the Company's executive management, including the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, also conducted an evaluation of the Company's internal control over financial reporting to determine whether any changes occurred

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during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Based on that evaluation, there have been no such changes during the period covered by this report.

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### Part II - Other Information

#### Item 1. Legal Proceedings

Not applicable

#### Item 2. Changes in Securities

Effective April 1, 2004, ACI Acquisition Corporation, a wholly-owned subsidiary of the Company, purchased all of the issued and outstanding stock of Airorlite Communications, Inc. The Company paid part of the purchase of Airorlite by issuing 37,000 shares of the Company's common stock valued at \$266,400. These shares were issued in reliance on the exemption provided by Section 4(2) of the Securities Act of 1933, as amended, as transactions not involving a public offering.

On July 28, 2004 the Company completed the \$3,300,000 private placement of its common stock to certain qualified institutional investors. Under the terms of the agreement, the Company sold 553,333 shares of common stock to the investors for \$6.00 per share. The Company also has granted the investors a warrant to acquire 138,333 shares of common stock at an exercise price of \$7.60 per share, exercisable for a period commencing six months after the date of issuance through the fifth anniversary of the issuance. In addition, the Placement Agent received a commission of 8% of the proceeds plus expenses and was issued a warrant to acquire 55,333 shares of common stock with the same terms as those issued to the institutional investors. After expenses, the net proceeds were approximately \$3,000,000.

During the three months ended June 30, 2004, several individuals exercised their employee incentive stock options. Through June 30, 2004, options to exercise 10,100 shares of the Company's common stock have been issued.

Subsequent to June 30, 2004, several individuals exercised their employee incentive stock options. Through August 13, 2004, options to exercise 9,425 shares of the Company's common stock have been issued.

#### 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

Not applicable

#### Item 6. Exhibits and Report on Form 8-K

(a) Exhibits

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| Number | Description   |
|--------|---|
| -----  | -----   |
| 10.1   | Securities Purchase Agreement*                                    |
| 10.2   | Registration Rights Agreement*                                    |
| 10.3   | Form of Warrant *   |
| 31(1)  | Rule 13a-14(a) 15d-14(a) Certification of Chief Executive Officer |
| 31(2)  | Rule 13a-14(a) 15d-14(a) Certification of Chief Operating Officer |
| 31(3)  | Rule 13a-14(a) 15d-14(a) Certification of Chief Financial Officer |
| 32     | Section 1350 Certification  |

\* Incorporated by reference to the 8K filed by the Company with the Securities and Exchange Commission on July 21, 2004

### (b) Reports on Form 8-K

On July 21, 2004, the Company filed an 8-K reporting on Item 2 event announcing that the Company issued a press release announcing a \$3,300,000 private placement.

On July 28, 2004, the Company filed an 8-K reporting on Item 2 event announcing that the Company issued a press release announcing completion of the \$3,300,000 private placement.

On August 11, 2004, the Company filed an 8-K reporting on Item 12 event announcing that the Company issued a press release announcing its financial results for the three and six months ended June 30, 2004.

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized

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### SIGNATURES

Date: August 13, 2004

/s/ JAMES E. HENRY

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James E. Henry  
Chairman, Chief Executive Officer,  
Treasurer and Director

Date: August 13, 2004

/s/ IRVIN F. WITCOSKY

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Irvin F. Witcosky  
Chief Operating Officer, President,  
Secretary and Director

Date: August 13, 2004

/s/ DOUGLAS WEST

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Douglas West  
Chief Financial Officer