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Class	Outstanding at June 30, 2002
Common stock, \$.01 par value	4,776,200

Diversified Security Solutions, Inc. and Subsidiaries

INDEX

Part I

Financial Information

Item 1.

Financial Statements

Consolidated Balance Sheets as of December 31, 2001 (Audited) and  
June 30, 2002 (Unaudited)

Consolidated Statements of Operations for the six and three months end  
June 30, 2002 (Unaudited) and June 30, 2001 (Unaudited)

Consolidated Statements of Cash Flows for the six  
months ended June 30, 2002 (Unaudited) and  
June 30, 2001 (Unaudited)

Notes to Financial Statements

Item 2.

Management's Discussion and Analysis of Financial Condition and Result  
Operations

Part II

Other Information

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## Diversified Security Solutions, Inc. and Subsidiaries Consolidated Balance Sheets

	As of	
	June 30, 2002 (Unaudited)	December 31, 2001 (Audited)
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 6,214,953	\$ 8,914,473
Accounts receivable - net	4,978,589	4,142,335
Securities held to maturity	403,028	802,235
Inventory	2,099,006	1,239,362
Costs in excess of billings	306,500	298,879
Deferred tax asset	88,400	88,000
Other assets	351,547	102,671
Total current assets	14,442,023	15,587,955
Property and equipment		
Accumulated depreciation	(1,019,197)	(882,222)
Computer software product costs	613,812	613,812
Accumulated amortization	(469,374)	(429,374)
Customer retainages	94,430	
Other assets	480,521	56,163
	\$15,957,792	\$16,301,518
Current liabilities		
Accounts payable	\$ 677,629	\$ 1,192,882
Accrued taxes and expenses	315,588	456,374
Income taxes payable	35,800	16,000
Billing in excess of cost	112,400	191,254
Long-term debt current		38,605
Capitalized leases current	8,159	10,642
Customer deposits	697,320	293,289
Total current liabilities	1,846,896	2,199,046
Long-term debt, less current	2,408,683	2,897,005
Deferred tax liability	103,000	103,000
	4,358,579	5,199,051
Stockholders' equity:		
Preferred stock - par value \$.01		
Common stock	47,762	47,250
Additional paid in capital	10,609,302	10,209,814
Deferred compensation	(10,417)	(20,834)
Retained earnings	952,566	866,237
Total stockholders' equity	11,599,213	11,102,467
	\$15,957,792	\$16,301,518

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## Diversified Security Solutions, Inc. and Subsidiaries Consolidated Statements of Operations

	Six months ended June 30,	
	2002	2001
	(UNAUDITED)	
Sales	\$7,394,016	\$6,209,405
Cost of goods sold	4,266,639	3,821,299
Gross profit	3,127,377	2,388,106
Operating expenses	2,935,706	2,016,338
Operating income	191,671	371,768
Interest:		
Income	(38,467)	0
Expense	78,809	93,203
Income before income taxes	151,329	278,565
Provision for income taxes	65,000	119,800
Net income	\$86,329	\$158,765
Basic and diluted earnings per share:		
Basic earnings per common share	\$0.02	\$0.05
Weighted average common share	4,725,000	3,000,000
Diluted earnings per common share	\$0.02	\$0.05
Weighted average diluted shares outstanding	4,800,000	3,075,000

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## Diversified Security Solutions, Inc. and Subsidiaries Consolidated Statements of Operations

	Three months ended June 30,	
	2002	2001
	(UNAUDITED)	
Sales	\$4,214,632	\$2,494,029
Cost of goods sold	2,375,295	1,517,859
Gross profit	1,839,337	976,170
Operating expenses	1,722,740	933,724
Operating income	116,597	42,446
Interest:		
Income	(9,471)	0
Expense	39,962	52,550
Income (loss) before income taxes	86,106	(10,104)
Provision for income taxes	39,000	4,800
Net income (loss)	\$47,106	(\$14,904)
Basic and diluted earnings per share:		
Basic earnings (loss) per common share	\$0.01	(\$0.00)
Weighted average common share	4,725,000	3,000,000
Diluted earnings (loss) per common share	\$0.01	(\$0.00)
Weighted average diluted shares outstanding	4,800,000	3,075,000

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## Consolidated Statements of Cash Flows

	For Six Months June 30 2002
<b>Cash Flows from Operating Activities:</b>	
Net income (loss) for the quarter	\$86,329
Adjustments to reconcile net income (loss) to net cash used in operating activities:	
Amortization of stock based compensation	10,417
Depreciation and amortization	176,975
Doubtful accounts expense	
Changes in operating assets and liabilities:	
Accounts receivable	(836,254)
Inventory	(859,644)
Costs in excess of billings	(7,621)
Prepaid Corp tax	(249,276)
Other assets	(115,767)
Accounts payable	(515,253)
Accrued taxes and expenses	(120,987)
Billings in excess of cost	(78,854)
Other liabilities	
Customer deposits held	404,031
Customer retainages	(94,430)
Net cash used in operating activities	(2,200,334)
<b>Cash Flows from Investing Activities:</b>	
Securities held to maturity	399,207
Computer software development costs	
Purchase of property and equipment and leasehold improv.	(368,984)
Cash provided by (used in) investing activities	30,223
<b>Cash Flows from Financing activities:</b>	
Proceeds of bank credit lines	
Proceeds of equipment loan facility	41,679
Repayments against bank credit lines	(530,000)
Repayments of loans from others	(38,605)
Capitalized lease obligation payments	(2,483)
Deferred IPO costs	0
Cash provided by financing (used in) activities	(529,409)
Net cash decrease	(2,699,520)
Cash-beginning	\$8,914,473
Cash-ending	\$6,214,953

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## Notes to Financial Statements

### Basis of Presentation

The financial information provided herein was prepared from the books and records of the Company without audit. The information furnished reflects all normal recurring adjustments, which, in the opinion of the Company, are necessary for a fair statement of the balance sheets, statement of operations, and statement of cash flows, as of the dates and for the Diversified Security Solutions, Inc. periods presented. The Notes to Financial Statements included in the Company's 2001 Annual Reports on Form 10-KSB should be read in conjunction with these financial statements.

The financial statements include operations of Photo Scan Systems, Inc. from April 1, 2002, which was acquired at May 17, 2002. See Item 2(d).

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

#### (a) Overview

We are a single source/turn-key provider of technology-based integrated security solutions for commercial enterprises and governmental agencies. Our two operating divisions are integration and manufacturing which focus on the electronic security of the security industry. We provide services, which include:

- o consulting and planning;
- o engineering and design;
- o systems integration; and
- o maintenance and technical support.

As a security integrator, we design, customize, install, connect and maintain Closed Circuit TV and access control systems for customers in the private and public sectors under the trade names, HBE and Henry Bros. Electronics. As part of an access control system, we may install, maintain and monitor intrusion alarms and sometimes monitor building system alarm for building maintenance systems and fire alarm systems.

We also manufacture, develop and assemble various related products, which we use in our own installations and for sales to other integrators under the trade name Viscom Products.

#### (b) Results of Operations

Comparison of three and six months ended June 30, 2002 to the three and six months ended June 30, 2001.

Revenues. Revenues for the quarter ended June 30, 2002 totaled \$4,214,632 representing an increase of 69.0% or \$1,720,603 from \$2,494,029 reported for the same quarter a year ago. Revenues for the six months ended June 30, 2002 totaled \$7,394,016 representing an increase of 19.1% or \$1,184,611 from \$6,209,405 reported for the same six months a year ago.

Revenues increased primarily due to customers releasing orders from existing

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backlog and new orders.

Cost of Goods Sold. Cost of Goods Sold for the quarter ended June 30, 2002 decreased by 4.5% to 56.4% of revenues for the quarter ended June 30, 2002, from 60.9% of revenues for the quarter ended June 30, 2001.

7

Cost of Goods Sold for the six months ended June 30, 2002 decreased by 3.8% to 57.7% of revenues for the six months ended June 30, 2002, from 61.5% of revenues for the six months ended June 30, 2001.

This reduction in cost was attributed to efficiency in both material purchase and labor utilization.

Selling, General and Administrative Expenses. Selling, General and Administrative Expenses increased to \$1,722,740 or 40.9% for the quarter ended June 30, 2002 from \$933,724 or 37.4% for the same quarter a year ago. For the six months ended June 30, 2002 Selling, General and Administrative Expenses increased to \$2,935,706 or 39.7% compared to \$2,016,338 or 32.5% for the six months ended June 30, 2001.

The increase in expenses was due mostly to the mobilization of the Company for growth. This includes new expenses for marketing and trade show attendance that was a nominal cost to the Company prior to January 1, 2002. In addition, new staffing and training for positions in sales project management and technical service has dramatically accelerated through the 2nd Quarter. This preparation in staffing and training will intended to enable the Company to meet the obvious challenge that an increase in business from the new proactive sales and marketing program may bring.

Operating Income. Operating Income for the quarter ended June 30, 2002 totaled \$116,597 or 2.8%, an increase of 1.1% or \$74,151 compared to \$42,446 or 1.7% for the same quarter a year ago. For the six months ended June 30, 2002, operating income decreased to \$191,671 or 2.6% compared to \$371,768 or 6.0% for the six months ended June 30, 2001.

The decrease in Operating Income was caused by the increased operating expenses due to additional sales, marketing, and project administrative hiring for the anticipated internal growth and acquisitions.

Interest Expense-net. Interest Expenses net of Interest Income for the three months ended June 30, 2002 was \$30,491 compared to \$52,550 for the comparable period a year ago. For the six months ended June 30, 2002 Interest expense-net decreased to \$40,342 compared to \$93,203 for the six months ended June 30, 2001. The savings were caused by no additional bank borrowing and \$9,471 in interest income for the quarter ended June 30, 2002, and no bank borrowing and \$38,467 in interest income for the six months ended June 30, 2002. Interest income was generated by short-term investment of the balance of the proceeds of the initial public offering on November 15, 2001.

Net Income. For the quarter ended June 30, 2002 our net income totaled \$47,106 or 1.1% of revenues, as compared to net loss of \$(14,904), or (0.6%) of revenues for the same period a year ago. For the six months ended June 30, 2001



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our net income totaled \$86,329 or 1.2% of revenues compared to \$158,765 or 2.6% of revenues for the same period a year ago. This resulted in basic earnings per share of \$0.02 on 4,725,000 basic weighted average common share outstanding for the six months ended June 30, 2002 compared with \$0.05 per share on 3,000,000 basic weighted average common shares outstanding for the six months ended June 30, 2001.

### (c) Liquidity and Capital Resources

Since our inception, we have financed our operations through bank debt, loans and equity from our principals, loans from third parties and funds generated by our business. On November 15, 2001, we successfully completed an initial public offering of 1,500,000 shares of our common stock. The public offering price of this offering was \$7.00 per share, and we received net proceeds of approximately \$8,613,014, after deducting the underwriter's discount of \$1,050,000 and offering expenses of \$836,986. In December, 2001, Gunn Allen Financial, Inc., the managing underwriter of our initial public offering, exercised its over-allotment option to purchase an additional 225,000 shares of common stock and we received net proceeds of \$1,370,250. As of June 30, 2002, we had \$6,214,953 in cash and cash equivalents and \$403,028 in short term bank certificate of deposit held to maturity.

8

Cash flows from Operating Activities. Net cash used in operating activities amounted to \$2,200,334 for the six months ended June 30, 2002 as compared to \$1,612,982 during the same period a year ago.

Cash flows from investing activities. Net cash provided by investing activities amounted to \$30,223 for the six months ended June 30, 2002 as compared to net cash used in investing activities of \$175,850 for the same period a year ago.

Cash flows from financing activities. Net cash used in financing activities amounted to \$529,409 for the six months ended June 30, 2002 as compared to net cash provided by financing activities amounted to \$1,268,611 for the same period a year ago.

Our capital requirements have grown substantially since our inception with the growth of our operations and staffing. We expect our capital requirements to continue to increase in the future as we seek to expand our operations. We believe that our current cash and available lines of credit should be sufficient to meet our capital requirements.

### (d) Acquisition

On May 17, 2002, we purchased all of the issued and outstanding shares of Photo Scan Systems, Inc. ("Photo Scan") from Secure Alarm Systems Inc. ("Secure Alarm"). Photo Scan is located in California, specializes in security systems for medical facilities and provides sales, system design, installation, service and maintenance of integrated security systems which include access control, closed circuit television, intercom, audio alarm and property intrusion

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detection. The purchase price for the issued and outstanding, shares of Photo Scan was \$600,000 of which \$200,000 was paid in cash and balance was paid by issuing 51,249 shares of our restricted common stock. Pursuant to the stock purchase agreement, we also paid off a \$200,000 note made by Photo Scan in favor of Secure Alarm. The stock purchase agreement provides that in the event that one year from May 17, 2002 (the "Reference Date"), the average closing sale price of our common stock for the ten trading days immediately prior to the Reference Date (the "Current Market Price") is less than approximately \$7.81 per share we will pay Secure Alarm an amount equal to the difference between \$400,000 and the 51,249 shares multiplied by the Current Market Price.

### (e) Recently Issued Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement No. 141 Business Combinations and Statement No.142 Goodwill and other Intangible Assets. These statements are effective July 1, 2001 for business combinations completed on or after that date. These statements became effective for us on January 1, 2002 with respect to business combinations completed on or before June 30, 2001.

### (f) Forward Looking Statements

This quarterly report contains certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to certain risks and uncertainties, including, among other things, doing business with governmental entities and the release of backlog orders, the fact that we face intense competition in a business characterized by rapid growth, changing technology and high capital requirements that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The Company wishes to advise readers that the factors listed above could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements. The Company does not undertake, and specifically declines any obligation, to publicly release the results of any revisions which may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

## Part II Other Information-

### Item 1. Legal Proceedings.

On or about April 18, 2002, Plaintiff Alan Carden commenced an action against, La Rossa ElectInc. Inc. and Henry Brothers., Inc. ("Henry Brothers"), our wholly-owned subsidiary, in Supreme Court of the State of New York, County of Westchester. The Complaint alleges that plaintiff was injured while working on the Westchester County Department of Correction while Henry Brothers was

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working on a job at the facility and as a result plaintiff is seeking \$6,000,000 together with costs and disbursements. We have submitted this matter to our insurance carrier.

Item 2. Changes in Securities

As stated above, on May 17, 2002, we purchased all of the issued and outstanding shares of Photo Scan Systems, Inc. ("Photo Scan"). The purchase price of the issued and outstanding shares of Photo Scan was \$600,000 of which \$200,000 was paid in cash and the balance was paid by issuing 51,259 shares of our restricted common stock to Secure Alarm. The issuance of the securities to Secure Alarm was in reliance on the exemption provided by Section 4(2) of the Securities Act of 1933, as amended as a transaction not involving a public offering.

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

Diversified Security Solutions, Inc.

By: /s/ James E. Henry

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James E. Henry  
Chairman and Chief Executive Officer

10

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, James E. Henry, Chairman and Chief Executive Officer of Diversified Security Solutions, Inc. (the "Company"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge the foregoing Quarterly Report of the Company:

1. fully complies with the requirements of section 13(a) or 15(d) of the Security Exchange Act of 1934, 15 U.S.C. 78 m or 78 o(d), and,
2. the information contained in the periodic report fairly present, in all material respects, the final condition and results of operations of the Company

Dated: August 13, 2002

James E. Henry  
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James E. Henry  
Chairman and Chief Executive Officer

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CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Louis Massad, Vice President and Chief Financial Officer of Diversified Security Solutions, Inc. (the "Company"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge the foregoing Quarterly Report of the Company:

1. fully complies with the requirements of section 13(a) or 15(d) of the Security Exchange Act of 1934, 15 U.S.C. 78 m or 78 o(d), and,
2. the information contained in the periodic report fairly present, in all material respects, the financial condition and results of operations of the Company

Dated: August 13, 2002

Louis Massad

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Louis Massad  
Vice President and Chief Financial Officer