

TRI-S SECURITY CORP
Form 10-Q/A
November 21, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

AMENDMENT NO. 1

on

FORM 10-Q/A

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

For the quarterly period ended March 31, 2005

o **TRANSITION REPORT UNDER SECTION 13 OR 15(d)**
OF THE EXCHANGE ACT

For the transition period from to

Commission file number 0-51148

TRI-S SECURITY CORPORATION

(Exact Name of Registrant as Specified in its Charter)

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GEORGIA
(State or Other Jurisdiction
of Incorporation or Organization)

30-0016962
(I.R.S. Employer Identification No.)

Royal Centre One, 11675 Great Oak Way, Suite 120, Alpharetta, GA 30022

(Address of Principal Executive Offices)

(678) 808-1540

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No .

Indicated by check mark whether registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act) Yes No .

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

Shares of the registrant's common stock, par value \$0.001 per share, outstanding as of May 11, 2005: 3,323,700.

EXPLANATORY NOTE

This Amendment No. 1 on Form 10-Q/A (the "Amendment") amends the Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (the "Original Report") of Tri-S Security Corporation (the "Company"). As reported in the Current Report on Form 8-K filed by the Company on November 2, 2005, the Audit Committee of the Company's Board of Directors determined that the Company's consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2004, the Original Report and the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2005 should be restated to account for the Company's 10% equity interest in Army Fleet Support, LLC, a joint venture which provides logistics support for U.S. Army aviation training at Fort Rucker, Alabama, using the equity method, rather than the cost method, of accounting as required by Account Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock* and Statement of Financial Accounting Standards No. 94, *Consolidation of All Majority-Owned Subsidiaries*.

The restated consolidated financial statements for the quarter ended March 31, 2005 included in the Amendment (the "Restatement") report a net loss \$439,000 as opposed to a net loss of \$46,000 as reported in the Original Report. See Note 2 of the Notes to Financial Statements included in the Amendment. The Amendment amends and restates Items 1, 2 and 4 of Part I and Item 6 of Part II of the Original Report to the extent necessary to reflect the effects of the Restatement. Except for such amendments, the Amendment continues to describe conditions as of the date of the Original Report, and the Company has not modified or updated other disclosures presented in the Original Report affected by subsequent events. Accordingly, the Amendment should be read in conjunction with the Original Report and the Company's filings made with the Securities and Exchange Commission subsequent to the filing of the Original Report.

TRI-S SECURITY CORPORATION

QUARTERLY REPORT ON FORM 10-Q

For the quarter ended March 31, 2005

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Tri-S Security Corporation and Subsidiary

Condensed Consolidated Balance Sheets

Unaudited

(In thousands, except per share data)

	March 31, 2005 (restated, Note 2)	December 31, 2004 (restated, Note 2)
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,853	\$ 313
Trade accounts receivable, net	4,782	5,312
Deferred initial public offering costs		633
Deferred income taxes	200	200
Prepaid expenses and other assets	974	178
Total current assets	7,809	6,636
Property and equipment, less accumulated depreciation	262	325
Note receivable - officer	102	100
Investment in joint venture	8,536	8,302
Investment in government contracts, net	1,073	1,172
Non compete agreements, net	304	318
Deferred loan cost, net		18
Goodwill	7,747	7,747
Total assets	\$ 25,833	\$ 24,618
Liabilities and Stockholders Equity (Deficit)		
Current liabilities:		
Trade accounts payable	\$ 139	\$ 351
Accrued salaries	1,022	774
Payroll and payroll withholding taxes	295	347
Accrued vacation	682	612
Accrued interest expense		316
Accrued interest on preferred stock subject to mandatory redemption	25	250
Other accrued expenses	1,275	689
Income taxes payable	572	212
Short-term notes payable	1,736	10,798
Current portion of capital lease obligations	92	91
Total current liabilities	5,838	14,440
Other liabilities:		
Capital lease obligations, less current portion	78	103
Income taxes payable	704	1,056
Deferred income taxes	3,246	3,287
Series C preferred stock subject to mandatory redemption	6,000	6,000
Total liabilities	15,866	24,886
Stockholders equity (deficit):		
Preferred stock, \$1.00 par value, 10,000,000 shares authorized		
Series A convertible preferred stock 100,000 shares issued and outstanding		460

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Series B convertible preferred stock, 40,000 shares issued and outstanding			196
Common stock, \$0.001 par value, 25,000,000 shares authorized, 3,285,000 and 827,832 shares issued and outstanding at March 31, 2004 and December 31, 2005, respectively		3	1
Additional paid-in capital		11,050	115
Retained earnings (deficit)		(1,086)	(1,040)
Total stockholders' equity (deficit)		9,967	(268)
Total liabilities and stockholders' equity (deficit)	\$	25,833	\$ 24,618

See accompanying notes to financial statements.

Tri-S Security Corporation and Subsidiary

Condensed Consolidated Statements of Operations

Unaudited

(In thousands, except per share data)

	Three Months Ended March 31 2005 (restated, Note 2)	Three Months Ended March 31 2004 (restated, Note 2)	Predecessor Basis Paragon Systems, Inc. January 1, 2004 to February 27, 2004
Revenues	\$ 7,979	\$ 2,578	\$ 4,705
Cost of revenues:			
Direct labor	4,216	1,264	2,481
Indirect labor and labor related costs	3,002	720	1,892
Other contract support costs	318	110	221
Amortization of government contracts	95	30	
	7,631	2,124	4,594
Gross profit	348	454	111
Selling, general and administrative	678	213	230
Operating income (loss)	(330)	241	(119)
Income from investment in joint venture	634	(10)	
Other income (expense):			
Interest income	12	1	
Interest expense	(315)	(174)	(11)
Interest on preferred stock subject to mandatory redemption	(75)	(25)	
	(378)	(198)	(11)
Income (loss) before income taxes	(74)	33	(130)
Income tax expense (benefit)	(28)	13	
Net income (loss)	\$ (46)	\$ 20	\$ (130)
Pro forma income tax expense (benefit)			(49)
Proforma net income (loss)			\$ (81)
Basic net income (loss) per common share	\$ (0.02)	\$ 0.02	
Diluted net income (loss) per common share	\$ (0.02)	\$ 0.02	
Basic weighted average number of common shares	2,358	825	
Diluted weighted average number of common shares	2,459	1,262	

See accompanying notes to financial statements.

Tri-S Security Corporation and Subsidiary

Condensed Consolidated Statements of Cash Flows

Unaudited

(In thousands)

	Three Months Ended March 31 2005 (restated, Note 2)	Three Months Ended March 31 2004 (restated, Note 2)	For the period January 1, 2004 to February 27, 2004
Cash flow from operating activities:			
Net income (loss)	\$ (46)	\$ 20	\$ (130)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:			
(Income) loss from investment in joint venture	(634)	10	
Depreciation and amortization	194	70	28
Deferred income tax benefits	(41)	(3)	
Changes in operating assets and liabilities:			
Trade accounts receivable, net	530	1,098	(1,161)
Prepaid expenses and other assets	(796)	15	(499)
Trade accounts payable	(212)	(363)	62
Accrued salaries	248	(36)	(59)
Payroll and payroll withholding taxes	(52)	(160)	226
Accrued vacation	70	17	85
Accrued interest expense	(316)	47	
Accrued interest on redeemable preferred stock	(225)	25	
Other accrued expenses	584	(294)	692
Income taxes payable	8	(38)	(111)
Net cash provided (used) by operating activities	(688)	408	(867)
Cash flow from investing activities:			
Acquisition of subsidiary		(2,300)	
Proceeds from investment in joint venture	400		715
Net cash provided (used) by investing activities	400	(2,300)	715
Cash flow from financing activities:			
Proceeds from initial public offering	11,079		
Proceeds (repayments) of short-term notes	(9,062)	2,902	(405)
Proceeds (repayments) of capital lease obligations	(24)	(7)	(13)
Deferred initial public offering costs	(165)		
Loan costs		(120)	
Net cash provided (used) by financing activities	1,828	2,775	(418)
Net increase (decrease) in cash and cash equivalents	1,540	883	(570)
Cash and cash equivalents at beginning of period	313	102	846
Cash and cash equivalents at end of period	\$ 1,853	\$ 985	\$ 276
Supplemental disclosures of cash flow information:			
Interest paid	\$ 931	\$ 148	\$ 6

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Income taxes paid	\$	6	\$	54	\$
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See accompanying notes to financial statements.

TRI-S SECURITY CORPORATION AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2005

1. Unaudited Financial Statements

The accompanying financial statements are unaudited and have been prepared by the management of Tri-S Security Corporation and subsidiary (the Company, Tri-S or we) in accordance with the rules and regulations of the Securities and Exchange Commission (the SEC). In the opinion of our management, all adjustments, consisting of normal recurring accruals necessary for the fair presentation of the financial position, results of operations and cash flows, have been included. For further information, refer to our audited financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2004 filed with the SEC (the Annual Report). Disclosure that substantially duplicates the disclosure contained in the footnotes to the audited financial statements included in the Annual Report has been omitted from these Notes.

2. Restatement

On October 27, 2005, the Audit Committee determined the Company's consolidated financial statements for the year ended December 31, 2004 and for the three months ended March 31, 2005 should be restated. The restatement is required for the Company's 10% equity interest in Army Fleet Support, LLC, to use the equity method of accounting as required by Account Principles Board Opinion No. 18, *The Equity Method of Accounting for Investment in Common Stock* and Statement of Financial Accounting Standards No. 94, *Consolidation of All Majority-Owned Subsidiaries*.

The following tables present the effect of the restatement on the originally reported financial position and results of operations as of and for the year ended December 31, 2004 and as of and for the three months ended March 31, 2005 and 2004. The originally reported cash flows from operating, investing, and financing activities were not affected.

	December 31, 2004 As Originally Reported	December 31, 2004 Restated	March 31, 2005 As Originally Reported	March 31, 2005 Restated
Balance Sheet:				
Current assets	\$ 6,636	\$ 6,636	\$ 7,809	\$ 7,809
Investment in joint venture	6,665	8,302	6,265	8,536
Other non-current assets	9,680	9,680	9,488	9,488
Total assets	\$ 22,981	\$ 24,618	\$ 23,562	\$ 25,833
Current liabilities	\$ 14,440	\$ 14,440	\$ 5,838	\$ 5,838
Other non-current liabilities	9,822	10,446	9,163	10,028

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Stockholders' equity (deficit)	(1,281)	(268)	8,561	9,967
Total liabilities and stockholders' equity	\$ 22,981	\$ 24,618	\$ 23,562	\$ 25,833

	Predecessor Basis Paragon Systems, Inc				
	Three Months Ended March 31, 2004 As Originally Reported	Three Months Ended March 31, 2004 Restated	January 1, 2004 to February 27, 2004	Three Months Ended March 31, 2005 As Originally Reported	Three Months Ended March 31, 2005 Restated
Statement of Operations:					
Revenues	\$ 2,578	\$ 2,578	\$ 4,705	\$ 7,979	\$ 7,979
Cost of revenues	2,124	2,124	4,594	7,631	7,631
Selling, general and administrative	213	213	230	678	678
Income from joint venture	0	(10)	0	0	634
Other income (expense)	(198)	(198)	(11)	(378)	(378)
Net income (loss) before income taxes	43	33	(130)	(708)	(74)
Income tax expenses (benefit)	16	13	0	(269)	(28)
Net income (loss)	\$ 27	\$ 20	\$ (130)	\$ (439)	\$ (46)
Basic net income (loss) per share	\$ 0.03	\$ 0.02	\$	\$ (0.19)	\$ (0.02)
Diluted net income (loss) per share	\$ 0.02	\$ 0.02	\$	\$ (0.19)	\$ (0.02)

3. Income Taxes

We account for our income taxes in accordance with Statement of Financial Accounting Standards No. 109. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax basis of assets and liabilities and their reported amounts and for operating loss carry forwards.

4. Initial Public Offering

On February 9, 2005, we commenced an underwritten initial public offering of 1,800,000 units (plus up to an additional 270,000 units subject to the exercise of the underwriters' over-allotment option), with each unit (a "Unit") consisting of one share of our common stock, par value \$0.001 per share (the "Common Stock"), and a warrant to purchase one share of Common Stock, at an initial offering price per Unit of \$6.00 (the "Initial Public Offering"). The Initial Public Offering closed with respect to the initial 1,800,000 Units on February 14, 2005 and with respect to the additional 270,000 Units on March 17, 2005. The aggregate net proceeds to us from the Initial Public Offering were approximately \$11,079,000 after underwriting discounts and commissions, offering expenses and consulting fees. As of December 31, 2004, we had accrued or paid \$633,000 in aggregate costs for the Initial Public Offering. Since December 31, 2004, we have accrued or paid an additional \$165,000 in aggregate costs for the Initial Public Offering.

5. Acquisition of Paragon Systems, Inc.

On February 27, 2004, Tri-S acquired (the Acquisition) all of the outstanding capital stock of Paragon Systems, Inc., an Alabama corporation with offices located in Huntsville, Alabama (Paragon Systems). At the closing of the Acquisition, we: (i) paid \$10.0 million, of which \$2.3 million was paid in cash and \$7.7 million was paid through the issuance of promissory notes (the Paragon Notes) to the former shareholders of Paragon Systems; and (ii) issued 100 shares of our Series C Redeemable Preferred Stock, with an aggregate redemption value of \$6.0 million. After the completion of the Initial Public Offering, we paid the outstanding principal of the Paragon Notes and all unpaid, accrued interest thereon. We are obligated to redeem the outstanding shares of Series C Redeemable Preferred Stock by February 27, 2007.

6. Common and Preferred Stock

On February 7, 2005, we effected an exchange and recapitalization (the Exchange and Recapitalization) of all the outstanding shares of our Common Stock, Series A Convertible Preferred Stock and Series B Convertible Preferred Stock and all rights to acquire our Common Stock pursuant to an Exchange and Recapitalization Agreement dated November 19, 2004 among the Company and all of the holders of the outstanding Common Stock, Series A Convertible Preferred Stock and Series B Convertible Preferred Stock and the holders of all rights to acquire Common Stock. As a result of the Exchange and Recapitalization, all of the outstanding shares of Common Stock, Series A Convertible Preferred Stock and Series B Convertible Preferred Stock were exchanged for an aggregate of 1,200,000 shares of Common Stock. The Exchange and Recapitalization was given retroactive treatment in the financial statements and related disclosures.

As of March 31, 2005, we are authorized to issue ten million shares of our preferred stock, par value \$1.00 per share (the Preferred Stock). Our Board of Directors is authorized, without further shareholder action, to divide any or all shares of authorized Preferred Stock into series and to fix and determine the designations, preferences and relative participating, optional or other special rights, and qualifications, limitations or restrictions thereon, of any series so established, including voting powers, dividend rights, liquidation preferences, redemption rights and conversion or exchange privileges.

As of December 31, 2004, we had outstanding 100,000 shares of Series A Convertible Preferred Stock, 40,000 shares of Series B Convertible Preferred Stock and 100 shares of Series C Redeemable Preferred Stock.

The shares of Series A Convertible Preferred Stock have no voting rights, except as otherwise required by applicable law, and no preemptive, dividend or sinking fund rights. In the Exchange and Recapitalization, all of the outstanding shares of Series A Convertible Preferred Stock were exchanged for an aggregate of 242,718 shares of Common Stock.

The shares of Series B Convertible Preferred Stock have no voting rights, except as otherwise required by applicable law, and no preemptive, dividend or sinking fund rights. In the

Exchange and Recapitalization, all of the outstanding shares of Series B Convertible Preferred Stock were exchanged for an aggregate of 129,450 shares of Common Stock.

The shares of Series C Redeemable Preferred Stock have no voting rights, except as otherwise required by applicable law, and no preemptive, conversion or sinking fund rights. In the event of a liquidation, dissolution or winding up of the Company, holders of the Series C Redeemable Preferred Stock are entitled to a liquidation preference and the holders of shares of Common Stock have a secondary liquidation right to the assets of the Company.

The Series C Redeemable Preferred Stock has a redemption value of \$60,000 per share. We may redeem the outstanding shares of Series C Redeemable Preferred Stock at any time, but must redeem all the outstanding shares of Series C Redeemable Preferred Stock no later than February 27, 2007. The holders of the Series C Redeemable Preferred Stock are entitled to receive cumulative cash dividends at a rate of 5% of the redemption value per annum (or \$300,000 per share per annum).

We are authorized to issue 25 million shares of Common Stock. The holders of Common Stock are entitled to one vote per share on all matters. The Common Stock does not have cumulative voting rights. Each share of Common Stock has an equal and ratable right to receive dividends to be paid from assets legally available when and if declared by our Board of Directors. We have never paid any cash dividends on the Common Stock.

7. Contingencies

Based on currently known facts, we believe there are no claims or litigation pending against us the disposition of which would materially affect our financial position or future operating results, although we cannot be certain as to the ultimate outcome of any such claim or litigation. In addition, exposure to litigation is inherent in our ongoing business and may harm our business in the future.

8. Investment in Unconsolidated Affiliate

In conjunction with the Paragon Systems, Inc. acquisition on February 27, 2004, the Company acquired a 10% interest in the Army Fleet Service Joint Venture. The value of the investment in the joint venture at the acquisition date was \$8,102 as established through an independent appraisal. The Company amortizes the cost of its investment in the joint venture using a 10 year life which approximates the anticipated life of the joint venture.

The Company accounts for its investment in the joint venture using the equity method. Accordingly, the investment in the joint venture is increased by the Company's share of the joint venture's earnings and reduced by the amortization of the investment in the joint venture and the cash received from the joint venture.

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The investment in the joint venture was effected by the following transactions for the three months ended March 31, 2005 and the one month ended March 31, 2004:

	Three Months Ended March 31, 2005	One Month Ended March 31, 2004
Investment in joint venture Beginning	\$ 8,302	\$ 8,102
Company's interest in earnings of the joint venture	840	59
Amortization of the investment in the joint venture	(206)	(69)
Cash received from the joint venture	(400)	
Investment in joint venture Ending	\$ 8,536	\$ 8,092

Summarized unaudited balance sheet information for the joint venture as of March 31, 2005 and December 31, 2004 is as follows:

	March 31, 2005	December 31, 2004
Total Assets	\$ 50,268	\$ 39,189
Total Liabilities	\$ 34,879	\$ 28,200
Equity	15,389	10,989
Total Liabilities and Equity	\$ 50,268	\$ 39,189

Summarized unaudited statement of operations information for the unconsolidated joint venture for the 3 months ended March 31, 2005 and 1 month ended March 31, 2004 is as follows:

	Three Months Ended March 31, 2005	One Month Ended March 31, 2004
Contract revenues	\$ 77,964	\$ 22,012
Operating income	8,424	602
Net earnings	8,401	590

9. Subsequent Event

On April 20, 2005, Paragon Systems entered into a new Factoring and Security Agreement with LSQ Funding Group, L.L.C. (LSQ) which amends Paragon Systems' existing factoring agreement with LSQ to increase Paragon Systems' available credit line to \$6.5 million and to decrease the effective borrowing rate on such credit line.

**Item 2:
Operations**

Management's Discussion and Analysis of Financial Condition and Results of

Certain information included in this Quarterly Report on Form 10-Q/A for the quarter ended March 31, 2005 (the Quarterly Report) contains, and other reports or materials we have filed or will file with the SEC (as well as information included in oral statements or other written statements made or to be made by us) contain or will contain, forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), Section 27A of the Securities Act of 1933, as amended (the Securities Act), and pursuant to the Private Securities Litigation Reform Act of 1995 (the PSLRA). Such forward-looking statements may relate to financial results and plans for future business activities, and are thus prospective. Such forward-looking statements are subject to risks, uncertainties, and other factors that could cause actual results to differ materially from future results expressed or implied by such forward-looking statements. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements are loss of customers, failure of customers to renew or extend existing contracts for security guard services and the risk factors detailed from time to time in our periodic reports and registration statements filed with the SEC. All forward-looking statements are made pursuant to the PSLRA and as such speak only as of the date made.

The results of operations presented or discussed below are based on historical results for the Company. Historical amounts for the three months ended March 31, 2004 and the period from January 1, 2004 to February 27, 2004 for Paragon Systems prior to the Acquisition are combined for presentation and discussion purposes.

Paragon Systems was formerly a subchapter S corporation and, consequently, pro forma income tax expense and pro forma net income are presented on the face of the historical statements for the period from January 1, 2004 to February 27, 2004. The adjustments include only taxes at a statutory rate of 38%.

Overview

We provide contract guard services to various Federal government agencies. These guard services include providing uniformed and armed guards for access control, personnel protection, plant security, theft prevention, surveillance, vehicular and foot patrol, crowd control and prevention of sabotage, terrorist and criminal activities. In connection with providing these services, we assume responsibility for a variety of functions, including recruiting, hiring, training and supervising security guards deployed to the Federal agencies served as well as paying all guards and providing them with uniforms, employee benefits and workers' compensation insurance. We are responsible for preventing the interruption of guard services as a consequence of illness, vacations or resignations.

Results of Operations

Three Months Ended March 31, 2005 Compared to Three Months Ended March 31, 2004

Revenue increased \$696,000 to \$7.9 million, or 9.6%, for the three months ended March 31, 2005, compared to revenue of \$7.3 million for the three months ended March 31, 2004. The increase in revenue resulted primarily from: (i) one new contract under which we started operations on October 1, 2004; (ii) additional services which were requested by the Federal Emergency Management Agency under a contract that we manage for the Department of Homeland Security primarily relating to hurricane Ivan which affected the Mobile, Alabama area in September 2004 (\$173,000); and (iii) existing contract cost increases which we are now allowed to bill to government agencies (\$458,000).

Cost of revenue increased \$913,000 to \$7.6 million, or 13.6%, for the three months ended March 31, 2005, compared to cost of revenue of \$6.7 million for the three months ended March 31, 2004. Amortization of our investment in government contracts accounts for \$65,000 of the increased cost and the new contract which started on October 1, 2004 accounts for another \$56,000. The remaining \$792,000 of increased cost of managing our government contracts relates to previously existing contracts. Labor and labor related cost of the previously existing contracts increased by \$805,000, offset by a reduction in other contract support cost of \$13,000. Our contracts with government agencies generally allow us to invoice certain increased cost to our government agency customers. We have not been allowed to invoice one of our customers, the Department of Homeland Security, for all of our cost of providing additional services to it relating to hurricane Ivan. The increased cost incurred by us during the three months ended March 31, 2005 due to providing assistance relating to hurricane Ivan which we were not allowed to recover totals \$35,000 in travel expenses. We intend to file a claim with the Department of Homeland Security to recover these additional expenses. In addition to the increased costs relating to hurricane Ivan, we have not been allowed to invoice certain of our increased labor costs relating to contracts with Department of Homeland Security even though our contracts with Department of Homeland Security provide for us to recover these increased labor costs. For the three months ended March 31, 2005, this amounts to approximately \$55,000. We intend to file a claim with the Department of Homeland Security to recover these costs plus similar costs for 2004 that we have not been allowed to invoice. Our gross profit on our contract with the Social Security Administration is \$103,000 less for the three months ended March 31, 2005 than the gross profit for the three months ended March 31, 2004. This primarily relates to increased cost of our labor that we were not able to pass on to the Social Security Administration. We are in the initial stages of evaluating our options as they relate to this contract.

Our gross profit decreased by \$217,000 for the three months ended March 31, 2005. This decrease is primarily attributable to increased amortization of government contracts of \$65,000 and to an increase in the cost of providing guard services of \$174,000 that we were not able to invoice to our government agency customers. The increase in the cost of providing guard services primarily relates to two contracts with the Department of Homeland Security and one with the Social Security Administration.

Selling, general and administrative expenses increased \$235,000 to \$678,000, or 53%, for the three months ended March 31, 2005 compared to \$443,000 for the three months ended March 31, 2004. The increase in costs for three months ended March 31, 2005 is attributable primarily to costs associated with the corporate office of Tri-S. In the three months ended March 31, 2005, corporate office expense includes the cost of additional staff and other costs related to, and legal, accounting and other professional fees associated with, being a public company. There were no similar costs incurred for the three months ended March 31, 2004.

Income from the Army Fleet Support, JV increased by \$644,000 to \$634,000 for the three months ended March 31, 2005 compared to the three months ended March 31, 2004. The \$634,000 is a result of \$840,000 of net earnings from the joint venture, less \$206,000 of amortization expense for the difference between our cost and our share of the net equity of the joint venture. In the three months ended March 31, 2004, we recognized \$59,000 of net earnings from the Joint Venture, less \$69,000 of amortization expense.

Interest expense increased \$180,000 to \$390,000 for the three months ended March 31, 2005 compared to interest expense of \$210,000 for the three months ended March 31, 2004. Interest expense of \$390,000 and \$210,000 for the three months ended March 31, 2005 and 2004, respectively, is almost entirely related to the Acquisition. In February 2005, we completed our Initial Public Offering and received proceeds therefrom before expenses of \$11.1 million. We used the proceeds from the Initial Public Offering to pay the Paragon Notes and to pay down the liability to the Company's factor. In connection with the Acquisition, Paragon Systems entered into a factoring agreement with LSQ to finance a portion of the purchase price of Paragon Systems. It is anticipated that paying the Paragon Notes and the reduction of our obligation to LSQ will significantly reduce interest expense in future periods. Interest expense relating to the Series C Redeemable Preferred Stock will continue to accrue interest at the rate of \$25,000 per month.

Income taxes are provided at 38% of income (loss) before income taxes. The 38% rate equals federal income taxes at 34% plus 4% for state income taxes net of the Federal effect. Paragon Systems used the cash basis of accounting for income taxes prior to the Acquisition on February 27, 2004. Pro forma income tax benefit at 38% is presented for comparative purposes. Even though Tri-S has a net operating loss carry forward of approximately \$1.8 million, we have recognized a deferred income tax benefit for the net operating loss carry forward because we anticipate reporting income before income taxes in future periods. In addition, cash distributions received from Army Fleet Support are taxable. We received cash distributions of \$400,000 and \$309,000 from Army Fleet Support in January 2005 and April 2005, respectively.

Liquidity and Capital Resources

Our current financial condition has been significantly influenced by four factors: (i) the successful completion of the Initial Public Offering; (ii) payment of the Paragon Notes; (iii) cash distributions received from Army Fleet Support; and (iv) reduction in our gross profit primarily attributable to three non-profitable contracts with Federal government agencies.

On February 9, 2005, we successfully completed the Initial Public Offering and realized proceeds of \$11.1 million. After paying the Paragon Notes totaling \$7.7 million, paying \$165,000 in additional costs of the Initial Public Offering and paying down our obligation to our factor, we retained approximately \$1.9 million to fund working capital, pay down other debt obligations, expand our operations and use for general corporate purposes.

We received \$400,000 and \$309,000 in cash distributions from our investment in Army Fleet Support in January 2005 and April 2005, respectively. We anticipate receiving similar quarterly distributions from Army Fleet Support over the next twelve months. We intend to use these cash distributions to make acquisitions, meet our income tax obligations resulting from the conversion of Paragon Systems from an S corporation to a C corporation for income tax purposes and for other general corporate purposes.

We reported cash out flow of \$688,000 from operating activities for the three months ended March 31, 2005. This results primarily from two factors: (i) payment of interest due on the Paragon Notes; and (ii) operating losses relating to three government contracts. Interest payments during the three months ended March 31, 2005 totaled \$706,000. On April 20, 2005, Paragon Systems executed a new agreement with our factor, LSQ, which should significantly reduce the cost of funds provided by LSQ for working capital purposes. We anticipate that the terms of the new agreement in combination with reduced borrowing will reduce our interest expense by approximately \$450,000 for 2005 compared to 2004. Operating losses on three of our government contracts totaled \$232,000. We are currently negotiating with the Department of Homeland Security to eliminate our operating losses on two of the contracts and to recover certain costs in prior years that should be covered based on terms of our contracts with the Department of Homeland Security.

Item 4: Controls and Procedures

In the Original Report, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by the Quarterly Report, our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) or 15d-15(e) of the Exchange Act) were effective. This conclusion was reached after our Chief Executive Officer and Chief Financial Officer evaluated our disclosure controls and procedures as of the end of the period covered by the Quarterly Report, as required by paragraph (b) of Rules 13a-15 or 15d-15 of the Exchange Act.

In connection with preparing the restated consolidated financial statements included in the Amendment, our Chief Executive Officer and Chief Financial Officer further evaluated our disclosure controls and procedures as of the end of the period covered by the Quarterly Report and concluded that such disclosure controls and procedures were ineffective because in the Original Report we accounted for our 10% equity interest in Army Fleet Support in accordance with cost method of accounting rather than the equity method of accounting.

During the quarter ended March 31, 2005, there was not any change in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 or 15d-15 of the Exchange Act that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 6.

Exhibits

The exhibits required to be filed with this Quarterly Report are set forth on the Exhibit Index attached hereto.

SIGNATURE

Pursuant to 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.

TRI-S SECURITY CORPORATION

Date: November 17, 2005

/s/ Ronald G. Farrell
Ronald G. Farrell
Chief Executive Officer
(duly authorized signatory and
Principal Executive Officer)

EXHIBIT INDEX

- 10.1 Factoring Agreement dated April 2005 between Paragon Systems, Inc. and LSQ Funding Group, L.L.C. (Incorporated by reference to Exhibit 99.1 to the Company's Form 8-K filed on April 26, 2005).
- 10.2 Form of Indemnification Agreement (Incorporated by reference to Exhibit 10.43 to the Company's Registration Statement on Form S-1, as amended (No. 333-119737)).
- 10.3 Summary of Board Compensation. (Previously filed.)
- 10.4 Federal Government Contract # DAAH 01-00-C-0057, as amended. (Previously filed.)
- 31.1 Rule 13a-14(a)/15d-14(a) Certification by the Company's Chief Executive Officer.
- 31.2 Rule 13a-14(a)/15d-14(a) Certification by the Company's Chief Financial Officer.
- 32.1 Section 1350 Certification by the Company's Chief Executive Officer.
- 32.2 Section 1350 Certification by the Company's Chief Financial Officer.
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