

**PARAGON TECHNOLOGIES, INC.**  
**Quarterly Report**  
For the Three Months Ended March 31, 2019



**A Delaware Corporation**

101 Larry Holmes Drive, Suite 500  
Easton, PA 18042

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SIC Codes: 3530 and 5045

**Quarterly Report**  
For the Period Ending: March 31, 2019  
(the "Reporting Period")

As of March 31, 2019, the number of shares outstanding of our Common Stock was: 1,704,745

As of December 31, 2018, the number of shares outstanding of our Common Stock was: 1,694,745

Indicate by check mark whether the company is a shell company (as defined in Rule 405 of the Securities Act of 1933 and Rule 12b-2 of the Exchange Act of 1934):

Yes:  No:

Indicate by check mark whether the company's shell status has changed since the previous reporting period:

Yes:  No:

Indicate by check mark whether a Change in Control of the company has occurred over this reporting period:

Yes:  No:

**PARAGON TECHNOLOGIES, INC.**  
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**1) Name of the issuer and its predecessors (if any)**

The name of the issuer is Paragon Technologies, Inc. ("Paragon" or the "Company").

The Company was originally incorporated in Pennsylvania on June 18, 1958 as SI Handling Systems, Inc.

On April 5, 2000, SI Handling Systems, Inc. changed its name to Paragon Technologies, Inc.

The Company changed its state of incorporation from Pennsylvania to Delaware on November 21, 2001. The Company is active and in good standing in Delaware.

Has the issuer or any of its predecessors ever been in bankruptcy, receivership, or any similar proceeding in the past five years?

Yes:  No:

**2) Security Information**

Trading symbol:	PGNT
Exact title and class of securities outstanding:	Common Stock
CUSIP:	69912T108
Par or stated value:	\$1.00 per share

Total shares authorized:	20,000,000	as of March 31, 2019
Total shares outstanding:	1,704,745	as of March 31, 2019
Number of shares in the Public Float:	907,857	as of March 25, 2019
Total number of shareholders of record:	184	as of March 25, 2019

Transfer Agent

Broadridge Shareholder Services  
Toll-free: (877) 830-4936  
Toll: (720) 378-5591  
Email: Kayur.Patel@broadridge.com

Is the Transfer Agent registered under the Exchange Act? Yes:  No:

Describe any trading suspension orders issued by the SEC concerning the issuer or its predecessors:

None

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off or reorganization either currently anticipated or that occurred within the past 12 months:

None

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**3) Issuance History**

**A. Changes to the Number of Outstanding Shares**

Check this box to indicate there were no changes to the number of outstanding shares within the past two completed fiscal years and any subsequent periods:

Number of Shares outstanding as of January 1, 2017		Opening Balance:							
		Common: 1,684,745 Preferred: 0							
Date of Transaction	Transaction type (e.g. new issuance, cancellation, shares returned to treasury)	Number of shares Issued (or cancelled)	Class of Securities	Value of shares issued (\$/per share) at issuance	Were the shares issued at a discount to market price at the time of issuance? (Yes/No)	Individual/Entity Shares were issued to (entities must have individual with voting / investment control disclosed).	Reason for share issuance (e.g. for cash or debt conversion) OR Nature of Services Provided (if applicable)	Restricted or Unrestricted as of this filing?	Exemption or Registration Type?
January 26, 2018	New issuance	10,000(1)	Common Stock	\$1.14	NO	Deborah Mertz	Compensation	Restricted, control security held by an officer of the Company(2)	Unregistered(3)
January 8, 2019	New issuance	10,000(1)	Common Stock	\$1.00	NO	Deborah Mertz	Compensation	Restricted, control security held by an officer of the Company(2)	Unregistered(3)
Shares Outstanding on March 31, 2019		Ending Balance:							
		Common: 1,704,745 Preferred: 0							

- (1) On each of January 26, 2018, and January 8, 2019, respectively, a stock grant of 10,000 shares was made to an employee of the Company.
- (2) All shares of common stock issued by the Company contain a restrictive legend since the shares are not registered with the Securities and Exchange Commission. Common stock must be held by non-affiliates for one year for the restrictive legend to be removed. Affiliates remain subject to the restrictions under Rule 144 promulgated under the Securities Act of 1933, as amended (the "Securities Act"), as long as they are affiliates of the Company and for 90 days thereafter.
- (3) Issued pursuant to an exemption from the registration requirements of the Securities Act, as provided by Rule 701, Regulation D and/or Section 4(a)(2) of the Securities Act, as applicable.

**B. Debt Securities, Including Promissory and Convertible Notes**

Check this box if there are no outstanding promissory, convertible notes or debt arrangements:

**4) Financial Statements**

A. The following financial statements were prepared in accordance with:

- U.S. GAAP
- IFRS

B. The financial statements for this reporting period were prepared by:

Name: Deborah Mertz  
Title: CFO  
Relationship to Issuer: Chief Financial Officer

**4) Financial Statements** *(Continued)*

The financial statements for the three months ended March 31, 2019 are incorporated by reference and can be found at the end of this Quarterly Report. The financial statements as of and for the three months ended March 31, 2019 include: (1) consolidated balance sheets, (2) consolidated statements of operations, (3) consolidated statements of comprehensive income, (4) consolidated statements of stockholders' equity, (5) consolidated statements of cash flows, and (6) notes to consolidated financial statements.

**5) Issuer's Business, Products and Services**

**A. Summary of the issuer's business operations**

**Business**

Paragon is a holding company owning subsidiaries that engage in diverse business activities including material handling, distribution, real estate, and investments.

**Automation**

Our material handling operations are operated through our subsidiary, SI Systems, LLC ("SI Systems"). SI Systems provides productivity enhancing material handling solutions, including complete systems, subsystem technologies, products, software and services for automated material handling and order processing applications. SI Systems' capabilities include horizontal conveyance, goods to man solutions, automated and semi-automated picking for order fulfillment, and a modular suite of high-performance Warehouse Execution Systems (WES) and Warehouse Management software. SI Systems supports both its install base and the broader industry install base with support, upgrade services, and aftermarket parts, as well as rejuvenation and retrofit engineering services.

We believe that SI Systems is known in the marketplace to have the most durable and maintenance free Towline solutions as well as the world's fastest automated order picking technologies. The newest additions to our material handling solution portfolio are the Mobile-Matic™ XL picking robot, a completely re-engineered Simon™ Automated Guided Vehicle, a solution set of Automated Storage and Retrieval technologies, and related software enhancements to complement. The new additions were added to support a broader customer demand for flexible automation solutions and address market gaps in our existing offerings.

SI Systems' automated material handling systems are currently used by manufacturing, assembly, order fulfillment, and distribution operations customers located primarily in North America, including the U.S. government. Our markets are diverse, and our customers and prospects represent leading manufacturer brands and their supply chain partners in the logistics services space. We sell our products directly and through integration partners.

SI Systems' business is largely dependent upon a limited number of large contracts with a limited number of customers. This dependence can cause unexpected fluctuations in sales volume. Various external factors affect the customers' decision-making process on expanding or upgrading their current production or distribution sites. Customers' timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. SI Systems believes that its business is not subject to seasonality, although the rate of new orders can vary substantially from month to month. Since the Company recognizes sales on a percentage of completion basis for its systems contracts, fluctuations in SI Systems' sales and earnings occur with increases or decreases in major installations.

**5) Issuer's Business, Products and Services:** *(Continued)*

**A. Summary of the issuer's business operations:** *(Continued)*

**Distribution**

Our distribution operations are carried out through our subsidiary SED International de Colombia, S.A.S. ("SED Colombia" or "SEDC"). SED Colombia currently distributes IT hardware products from 27 top worldwide leading IT manufacturers such as Hewlett Packard, Lenovo, Dell, Samsung, LG, Epson, Ricoh and others.

SEDC business is divided into three main business units: Value, Transactional and Integrated Services. The Value business unit focuses on enterprise sales and business projects, typically selling more specialized products that usually carry higher margins. The top products distributed by our Value unit include servers, workstations, storage, networking, high-end printers, high-end audio visual and power protection systems.

The SEDC Transactional business unit focuses on the consumer business (retail resellers / e-tailers) as well as run rate products for Value Added Resellers (VARs) selling to small and medium businesses (SMB). The top products distributed by the Transactional business unit include notebook computers, desktop computers, printers, TVs, audio/visual equipment, projectors, gaming and accessories.

The services provided by our Integrated Service business unit include managed services, printing outsourcing, electronic documents management, electronic invoicing and IoT. The Integrated Service unit has also taken ownership of the extended warranties and maintenance agreements sales.

**Real Estate**

In December 2017, Ohana Home Services, LLC, a wholly owned subsidiary of Paragon, was established to acquire real estate for income and capital appreciation purposes. In December 2017, Paragon acquired residential real estate in Las Vegas, Nevada for \$750,000. In January 2018, Paragon transferred title of the real estate to Ohana. There was no consideration exchanged between the parties. In January 2018, Ohana acquired a second similar residential property also in Las Vegas, Nevada for \$750,000. Ohana intends to lease its real estate to generate positive cash flow for the foreseeable future and may seek to monetize its real estate holdings during favorable market conditions.

**Investments**

Paragon also invests in businesses and securities under the Investment Management Policy. The Investment Management Policy sets forth the parameters under which a portion of Paragon's cash balance may be invested in marketable securities, including U.S. Treasuries, equities of publicly traded companies, bonds, money market instruments and other securities. Investment decisions under the Investment Management Policy are made by Hesham Gad, Chairman and Chief Executive Officer. The Investment Management Policy sets forth restrictions on the investment of Paragon's funds, including an aggregate limit on Paragon's cash balance that is made available for investment, limits on the amount that may be invested in any single equity or fixed income position or certain categories of securities, prohibition of short-selling, margin trading and the use of leverage, requirements for the management of the investment account, and other Board-approval requirements.

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**5) Issuer's Business, Products and Services** *(Continued)*

**B. Describe subsidiaries, parents or affiliated companies**

The Company has the following wholly owned subsidiaries: (1) SI Systems, LLC; (2) Ohana Home Services, LLC; and (3) ARK Investments, LLC. The officers of all three are: Hesham Gad, President and CEO; and Deborah Mertz, CFO. The business address of all three is 101 Larry Holmes Drive, STE 500, Easton, PA 18042.

ARK Investments, LLC owns 80% of SED International de Colombia, S.A.S. (SEDC). Ronell Rivera is President of SEDC, which is located at Parque Industrial Gran Sabana Bodega 31, Vereda Tibitó – Tocancipá.

**C. Describe the issuers' principal products or services and their markets**

For information regarding our principal products or services and their markets, please see Section 5.A. above.

**6) Issuer's Facilities**

Paragon Technologies, Inc.  
101 Larry Holmes Drive, Suite 500  
Easton, PA 18042

SI Systems leases a facility located at 101 Larry Holmes Drive in Easton, Pennsylvania. The area covered by the lease is 9,648 square feet. The leasing agreement requires fixed monthly payments of \$14,400 through April 30, 2020, when the lease expires.

SI Systems believes that its Easton, Pennsylvania facility is adequate for its current operations. SI Systems' operations experience fluctuations in workload due to the timing and receipt of new orders and customer job completion requirements. Currently, SI Systems' facility is adequate to handle these fluctuations. In the event of an unusual demand in workload, SI Systems supplements its internal operations with outside subcontractors that perform services for SI Systems in order to complete contractual requirements for its customers. SI Systems will continue to utilize internal personnel and its own facility and, when necessary and/or cost effective, outside subcontractors to complete contracts in a timely fashion in order to address the needs of its customers.

SED Colombia leased a 32,000 square foot facility in Chia (Cundinamarca), Colombia. The center, located near Bogotá, the capital city of Colombia, serves as a sales and administrative office and distribution facility for SEDC. The lease expired in October 2018. The monthly payment was the equivalent of approximately \$9,951. On January 1, 2019, SED Colombia entered into a five year lease agreement for a 44,530 square foot facility in Tocancipa (Cundinamarca) to serve as its new sales and administrative office and distribution facility. The new monthly payment is the equivalent of approximately \$14,174. SEDC continued to rent the Chia facility on a month to month basis until all departments were transferred to the new building. All departments vacated the Chia facility by April 30, 2019.

SEDC also leases office #210 at 14707 South Dixie Highway in Palmetto Bay, Florida. The lease expired at the end of March 2019 and was renewed for an additional year for a monthly payment of \$1,378. In addition, SEDC rents two apartments in Chia for the use of its two members of its management team based out of Miami, Florida for an aggregate monthly payment of the equivalent of approximately \$908. One lease expired at the end of March 2019 and was replaced with a lease on a house in Chia for a monthly payment of approximately \$970, expiring mid-March 2020. The other lease expires in mid-July 2019 and will not be renewed.

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**7) Officers, Directors, and Control Persons**

Name of Officer/Director and Control Person	Affiliation with Company (e.g. Officer/Director/Owner of more than 5%)	Residential Address (City / State Only)	Number of shares owned	Share type/class	Ownership Percentage of Class Outstanding	Note
Hesham M. Gad	Director, Officer & Owner of >5%	C/O Paragon Technologies 101 Larry Holmes Drive Suite 500 Easton, PA 18042	520,408	Common stock	30.5%	
Donna Van Allen & Van Allen Investments	Owner of >5%	Winter Springs, Florida	245,000	Common Stock	14.4%	
William Guegel	Owner of >5%	Pearland, TX	125,064	Common Stock	7.3%	
Kevin Ting	Owner of >5%	Mission Viejo, CA	90,352	Common Stock	5.3%	
Deborah Mertz	Officer	C/O Paragon Technologies 101 Larry Holmes Drive Suite 500 Easton, PA 18042	20,000	Common Stock	1.2%	
Jack H. Jacobs	Director	C/O Paragon Technologies 101 Larry Holmes Drive Suite 500 Easton, PA 18042	5,740	Common Stock	0.3%	
Samuel S. Weiser	Director	C/O Paragon Technologies 101 Larry Holmes Drive Suite 500 Easton, PA 18042	5,740	Common Stock	0.3%	

Name, Other Positions or Offices With the Company and Principal Occupation for Past Five Years	Director Since	Age
Hesham M. Gad .....	2010	41

**Hesham M. Gad** has been Chief Executive Officer of the Company since June 2014, Chairman of the Company's Board of Directors since March 2012 and a director of the Company since October 2010. From 2013 to 2017 Mr. Gad served as Chairman and CEO of SED International Holdings, a multinational distributor of IT and computing products.

Mr. Gad is also the author of the internationally published book, "The Business of Value Investing." Mr. Gad holds a B.A. in finance and an MBA in finance from the University of Georgia.

**7) Officers, Directors, and Control Persons (Continued)**

Jack H. Jacobs ..... 2012 73

**Jack H. Jacobs** is the Melcher Family Chair and Professor of Humanities and Public Affairs at the United States Military Academy at West Point, where he has been teaching since 2005, and a principal of The Fitzroy Group, Ltd., a firm that specializes in the development of residential real estate in London and invests both for its own account and in joint ventures with other institutions, for over 20 years. He has served as an on-air military analyst for NBC News since 2002, where he was an Emmy nominee in 2010 and 2011 and a recipient of the 2011 Murrow Award. Colonel Jacobs was a co-founder and Chief Operating Officer of AutoFinance Group Inc., one of the firms to pioneer the securitization of debt instruments, from 1988 to 1989; the firm was subsequently sold to KeyBank. He was a Managing Director of Bankers Trust Corporation, a diversified financial institution and investment bank, where he ran foreign exchange options worldwide and was a partner in the institutional hedge fund business.

Colonel Jacobs' military career included two tours of duty in Vietnam where he was among the most highly decorated soldiers, earning three Bronze Stars, two Silver Stars and the Medal of Honor, the nation's highest combat decoration. He retired from active military duty as a Colonel in 1987. Colonel Jacobs has been a member of the board of directors of Datatrak International, Inc. (OTCMKTS: DTRK) since 2016, Resonant Inc. (Nasdaq: RESN) since 2018, and Ballantyne Strong, Inc. (NYSE American: BTN) since 2018. From 2007 to 2012, Colonel Jacobs served as a member of the Board of Directors of Xedar Corporation, a public company; from June 2006 to 2009, he was a director of Visual Management Systems, a private company; and he was a director of BioNeutral Group, Inc., a public company, until 2009. From October 17, 2013 to October 28, 2013, Colonel Jacobs served on the board of SED International Holdings, Inc. He was previously a director of Premier Exhibitions, Inc. Colonel Jacobs is Co-Chairman of the Medal of Honor Foundation and a member of the Board of Trustees of the USO of New York. He is the author of the book "If Not Now, When?: Duty and Sacrifice in America's Time of Need." Colonel Jacobs received a Bachelor of Arts and a Master's degree from Rutgers University.

Samuel S. Weiser ..... 2012 59

**Samuel S. Weiser** is currently the President and Chief Executive Officer of Foxdale Management LLC, a consulting firm founded by Mr. Weiser that provides operational consulting, strategic planning, and litigation support services in securities related disputes, which has been operating since 2003. From August 2009 until April 2015, he was a member of the Board of Directors and from August 2014 until March 2015 was Executive Chairman of Premier Exhibitions, Inc., a provider of museum quality touring exhibitions then listed on Nasdaq. In addition, Mr. Weiser served as President and Chief Executive Officer of Premier Exhibitions from November 2011 until June 2014. Mr. Weiser was a member of SED International's Board of Directors from October of 2013 until October 2014. Previously, Mr. Weiser served as a member and Chief Operating Officer of Sellers Capital LLC, an investment management firm, from 2007 to 2010. From 2005 to 2007, he was a Managing Director responsible for the Hedge Fund Consulting Group within Citigroup Inc.'s Global Prime Brokerage Division. Mr. Weiser also served as Chairman of the Managed Funds Association, a lobbying organization for the hedge fund industry, from 2001 to 2003 and was formerly a partner in Ernst and Young. He received his B.A. in Economics from Colby College and a M.A. in Accounting from George Washington University.

**PARAGON TECHNOLOGIES, INC.**  
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For the Period Ended March 31, 2019

**7) Officers, Directors, and Control Persons (Continued)**

The directors of the Company hold their positions as directors until the next Annual Meeting of Stockholders.

The names, ages, and offices with the Company of its executive officers are as follows:

<u>Name</u>	<u>Age</u>	<u>Office</u>
Hesham M. Gad	41	Chief Executive Officer, Paragon Technologies
Deborah R. Mertz	62	Chief Financial Officer, Paragon Technologies

**Deborah R. Mertz** is an accounting professional with over 40 years' experience in both publicly held and privately held companies. From 2006 to 2013, Ms. Mertz held the position of Assistant Controller of ASSA ABLOY Inc. Americas Division. ASSA ABLOY is the largest global supplier of intelligent lock and security solutions. From 1999 to 2006, Ms. Mertz was the Controller/CFO of Sargent Manufacturing Company. Sargent Manufacturing Company is a wholly owned subsidiary of ASSA ABLOY Inc. and manufactures architectural hardware used primarily in commercial construction. Ms. Mertz has held various other senior accounting positions. Ms. Mertz is a CPA and has an MBA from Rider University and a B.S. in Accounting from King's College.

**8) Legal/Disciplinary History**

A. Please identify whether any of the persons listed above have, in the past 10 years, been the subject of:

1. A conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses).

The executive officers and directors of the Company have not, in the past 10 years, been the subject of a conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses).

2. The entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended, or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities.

The executive officers and directors of the Company have not, in the past 10 years, been the subject of the entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities.

**8) Legal/Disciplinary History (Continued)**

3. A finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated.

The executive officers and directors of the Company have not, in the past 10 years, been the subject of a finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated.

4. The entry of an order by a self-regulatory organization that permanently or temporarily barred, suspended or otherwise limited such person's involvement in any type of business or securities activities.

The executive officers and directors of the Company have not, in the past 10 years, been the subject of the entry of an order by a self-regulatory organization that permanently or temporarily barred, suspended or otherwise limited such person's involvement in any type of business or securities activities.

The Company has no information regarding beneficial owners of more than 5% of its common stock other than Mr. Gad, the Chief Executive Officer and the Chairman of the Company's Board of Directors.

- B. Describe briefly any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the issuer or any of its subsidiaries is a party or of which any of their property is the subject. Include the name of the court or agency in which the proceedings are pending, the date instituted, the principal parties thereto, a description of the factual basis alleged to underlie the proceeding and the relief sought. Include similar information as to any such proceedings known to be contemplated by governmental authorities.

There have been no material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the issuer or any of its subsidiaries is a party or of which any of their property is a subject.

**9) Third Party Providers**

Please provide the name, address, telephone number, and e-mail address of each of the following outside providers:

Securities Counsel:

Name: Derek D. Bork  
Firm: Thompson Hine LLP  
Address 1: 3900 Key Center, 127 Public Square  
Address 2: Cleveland, Ohio 44114-1291  
Phone: (216) 566-5500  
Email: [Derek.Bork@thompsonhine.com](mailto:Derek.Bork@thompsonhine.com)

**PARAGON TECHNOLOGIES, INC.**  
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**9) Third Party Providers** *(Continued)*

Accountant or Auditor:

Name: Danielle Preston  
Firm: RSM US LLP  
Address 1: 518 Township Line Rd, Suite 300  
Address 2: Blue Bell, PA 19422  
Phone: (215) 641-8600  
E-mail: [Danielle.Preston@rsmus.com](mailto:Danielle.Preston@rsmus.com)

Investor Relations Consultant:

None.

Other Service Providers:

Provide the name of any other service provider(s), including counsel, advisor(s) or consultant(s), that assisted, advised, prepared or provided information with respect to this disclosure statement, or provided assistance or services to the issuer during the reporting period.

Name: Jose Luis Salgado C.  
Firm: RSM Colombia  
Nature of Services: Statutory Auditor: Colombia  
Address 1: Avenida Calle 26 N 69D – 91 Of.  
Address 2: 303 / 306 / 702A Torre Peatonal.  
Address 3: Centro Empresarial Arrecife.  
Address 4: Bogota, Colombia  
Phone: +57 (1) 410 4122  
E-mail: [jose.salgado@rsmco.co](mailto:jose.salgado@rsmco.co)

**PARAGON TECHNOLOGIES, INC.**  
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For the Period Ended March 31, 2019

**10) Issuer Certification**

*Principal Executive Officer*

I, Hesham M. Gad, Chief Executive Officer, certify that:

1. I have reviewed this quarterly disclosure statement of Paragon Technologies, Inc.;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

May 15, 2019

/s/ Hesham M. Gad

Hesham M. Gad  
Chief Executive Officer

*Principal Financial Officer*

I, Deborah R. Mertz, Chief Financial Officer, certify that:

1. I have reviewed this quarterly disclosure statement of Paragon Technologies, Inc.;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

May 15, 2019

/s/ Deborah R. Mertz

Deborah R. Mertz  
Chief Financial Officer

**PARAGON TECHNOLOGIES, INC.  
and Subsidiaries**

**QUARTERLY REPORT**  
**CONSOLIDATED FINANCIAL STATEMENTS – UNAUDITED FOR THE**  
**THREE MONTHS ENDED MARCH 31, 2019**

## CONSOLIDATED FINANCIAL STATEMENTS

# I N D E X

### •Consolidated Financial Statements:

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**PARAGON TECHNOLOGIES, INC.**  
Consolidated Balance Sheets (Unaudited)  
March 31, 2019 and December 31, 2018  
*(In Thousands, Except Share Data)*

<b>Assets</b>	March 31, 2019	December 31, 2018
Current assets:		
Cash and cash equivalents	\$ 1,207	\$ 1,522
Trade accounts receivables, net	12,983	14,080
Contract assets	29	338
Inventories:		
Raw materials	113	110
Work-in-process	-	1
Finished goods	14,281	13,247
Total inventories	14,394	13,358
Prepaid expenses and other current assets	4,455	3,066
Total current assets	33,068	32,364
Marketable securities	206	250
Property and equipment		
Real estate	1,500	1,500
Machinery and equipment	590	451
Software	448	434
Land	18	18
Leasehold Improvements	264	18
Capital Additions in Process	-	2
Less: accumulated depreciation	817	748
Net property and equipment	2,003	1,675
Right of use assets	1,150	-
Other assets - intangible assets, net	532	549
Deferred tax asset	230	224
Total assets	\$ 37,189	\$ 35,062

*See accompanying notes to consolidated financial statements.*

*(Continued)*

**PARAGON TECHNOLOGIES, INC.**  
Consolidated Balance Sheets (Unaudited) *(Continued)*  
March 31, 2019 and December 31, 2018  
*(In Thousands, Except Share Data)*

	March 31, 2019	December 31, 2018
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 18,200	\$ 20,019
Contract liabilities	1,342	1,290
Accrued salaries, wages, and commissions	305	310
Accrued product warranties	104	104
Income taxes payable	765	780
Accrued other liabilities	1,532	1,017
Operating lease	419	-
Bank loan - line of credit	7,094	4,977
Total current liabilities	<u>29,761</u>	<u>28,497</u>
Long term liabilities:		
Operating lease	731	-
Total liabilities	<u>\$ 30,492</u>	<u>\$ 28,497</u>
Commitments and contingencies (Notes 1 and 10)		
Stockholders' equity:		
Common stock, \$1 par value; authorized 20,000,000 shares; issued and outstanding 1,704,745 shares as of March 31, 2019 and 1,694,745 as of December 31, 2018	1,705	1,695
Additional paid-in capital	3,500	3,500
Retained earnings	1,162	1,139
Accumulated other comprehensive loss	(799)	(872)
Total Paragon Technologies, Inc. and subsidiaries stockholders' equity	<u>5,568</u>	<u>5,462</u>
Noncontrolling interest in subsidiary	1,129	1,103
Total stockholders' equity	<u>6,697</u>	<u>6,565</u>
Total liabilities and stockholders' equity	<u>\$ 37,189</u>	<u>\$ 35,062</u>

*See accompanying notes to consolidated financial statements.*

**PARAGON TECHNOLOGIES, INC.**

Consolidated Statements of Operations (Unaudited)  
For the Three Months Ended March 31, 2019 and 2018  
(In Thousands, Except Share and Per Share Data)

	Three Months Ended	
	March 31, 2019	March 31, 2018
Net sales	\$ 23,700	\$ 18,773
Cost of sales	21,697	17,063
Gross profit on sales	<u>2,003</u>	<u>1,710</u>
Operating expenses:		
Selling, general and administrative expenses	1,748	1,628
Product development costs	3	4
Total operating expenses	<u>1,751</u>	<u>1,632</u>
Operating income	<u>252</u>	<u>78</u>
Other income (expense)		
Interest income	4	3
Interest expense	(121)	(91)
Realized gain (loss) on investment, marketable securities	(11)	149
Unrealized gain on investment, equity securities	23	1
Total other income (expense), net	<u>(105)</u>	<u>62</u>
Income before income taxes and noncontrolling interest	147	140
Income tax expense	98	86
Net income before noncontrolling interest	49	54
Net income attributable to noncontrolling interest	26	23
Net income attributable to Paragon Technologies, Inc. and subsidiaries	<u>\$ 23</u>	<u>\$ 31</u>
Basic and diluted income per share	<u>\$ 0.01</u>	<u>\$ 0.02</u>
Weighted average shares outstanding	1,704,526	1,694,033
Dilutive effect of stock options	-	-
Weighted average shares outstanding assuming dilution	<u>1,704,526</u>	<u>1,694,033</u>

See accompanying notes to consolidated financial statements.

**PARAGON TECHNOLOGIES, INC.**

Consolidated Statements of Comprehensive Income (Unaudited)

For the Three Months Ended March 31, 2019 and 2018

(In Thousands)

	<u>Three Months Ended</u>	
	<u>March 31,</u> <u>2019</u>	<u>March 31,</u> <u>2018</u>
Net income	\$ 49	\$ 54
Other comprehensive income (loss):		
Unrealized income (loss) on debt securities, net of tax	(44)	21
Foreign currency translation	<u>117</u>	<u>357</u>
Comprehensive income	<u>\$ 122</u>	<u>\$ 432</u>

*See accompanying notes to consolidated financial statements.*

**PARAGON TECHNOLOGIES, INC.**

Consolidated Statements of Stockholders' Equity (Unaudited)

For the Three Months Ended March 31, 2019 and the years ended December 31, 2018 and 2017

(In Thousands, Except Share and Per Share Data)

	Common Stock		Additional Paid-Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest	Total Stockholders' Equity
	Shares	Amount					
Balance at January 1, 2017	1,684,745	1,685	3,499	(2,636)	259	-	2,807
Net income	-	-	-	2,740	-	882	3,622
Net change in unrealized loss on debt securities, net of tax	-	-	-	-	(470)	-	(470)
Restricted stock	-	-	-	-	-	209	209
Distribution	-	-	-	-	-	(51)	(51)
Foreign currency translation	-	-	-	-	(93)	-	(93)
Balance at December 31, 2017	1,684,745	1,685	3,499	104	(304)	1,040	6,024
Net Income	-	-	-	952	-	113	1,065
Net change in unrealized loss on debt securities, net of tax	-	-	-	-	(65)	-	(65)
Adoption of ASU 2016-01	-	-	-	83	(83)	-	-
Distribution	-	-	-	-	-	(50)	(50)
Foreign currency translation	-	-	-	-	(420)	-	(420)
Stock grants to employees	10,000	10	1	-	-	-	11
Balance at December 31, 2018	1,694,745	\$ 1,695	\$ 3,500	\$ 1,139	\$ (872)	\$ 1,103	\$ 6,565
Net Income	-	-	-	23	-	26	49
Net change in unrealized loss on debt securities, net of tax	-	-	-	-	(44)	-	(44)
Distribution	-	-	-	-	-	-	-
Foreign currency translation	-	-	-	-	117	-	117
Stock grants to employees	10,000	10	-	-	-	-	10
Balance at March 31, 2019	1,704,745	\$ 1,705	\$ 3,500	\$ 1,162	\$ (799)	\$ 1,129	\$ 6,697

See accompanying notes to consolidated financial statements

**PARAGON TECHNOLOGIES, INC.**

Consolidated Statements of Cash Flows (Unaudited)  
For the Three Months Ended March 31, 2019 and 2018  
(In Thousands)

	March 31, 2019	March 31, 2018
Cash flows from operating activities:		
Net income	\$ 49	\$ 54
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property and equipment	53	32
Amortization of intangible assets	17	17
Amortization of the right of use assets	(82)	-
Change in lease liability	82	-
Realized gain (loss) on investments	11	(149)
Unrealized gain on investments	(23)	(1)
Stock based compensation	10	11
Deferred taxes	16	48
Change in operating assets and liabilities:		
Trade accounts receivables	1,096	2,049
Contract assets	309	18
Inventories	(1,036)	(686)
Prepaid expenses and other current assets	(1,389)	(44)
Accounts payable	(1,819)	(1,603)
Contract liabilities	52	(348)
Accrued salaries, wages and commissions	(5)	31
Income tax payable	(15)	(391)
Accrued product warranties	-	14
Accrued other liabilities	513	(471)
Net cash used in operating activities	<u>(2,161)</u>	<u>(1,419)</u>
Cash flows from investing activities:		
Purchases of property and equipment	(377)	(793)
Purchases of investments	(11)	-
Proceeds from sale of investments	8	325
Net cash used in investing activities	<u>(380)</u>	<u>(468)</u>
Cash flows from financing activities:		
Borrowings of bank loan - line of credit, net	2,117	517
Noncontrolling interest distribution	-	(50)
Net cash provided by financing activities	<u>2,117</u>	<u>467</u>
Effect of exchange rates on cash	109	328
Decrease in cash and cash equivalents	(315)	(1,092)
Cash and cash equivalents, beginning of period	1,522	2,039
Cash and cash equivalents, end of period	<u>\$ 1,207</u>	<u>\$ 947</u>
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest expense	<u>\$ 97</u>	<u>\$ 89</u>
Income taxes	<u>\$ -</u>	<u>\$ -</u>
Supplemental disclosures of noncash investing activities:		
Mark to market on available for sale securities, gross	<u>\$ (36)</u>	<u>\$ (110)</u>
Supplemental disclosures of noncash operating, investing and financing activities:		
Acquisition of business (Note 2)		

*See accompanying notes to consolidated financial statements.*

## **(1) Description of Business and Summary of Significant Accounting Policies**

### **Description of Business and Concentrations of Credit Risk**

Paragon Technologies, Inc. (“Paragon” or the “Company”) is a holding company owning subsidiaries that engage in diverse business activities including material handling, distribution, real estate, and investments.

### **Automation**

Our material handling operations are operated through our subsidiary, SI Systems, LLC (“SI Systems”). SI Systems provides productivity enhancing material handling solutions, including complete systems, subsystem technologies, products, software and services for automated material handling and order processing applications. SI Systems’ capabilities include horizontal conveyance, goods to man solutions, automated and semi-automated picking for order fulfillment, and a modular suite of high-performance Warehouse Execution Systems (WES) and Warehouse Management software. SI Systems supports both its install base and the broader industry install base with support, upgrade services, and aftermarket parts, as well as rejuvenation and retrofit engineering services.

We believe that SI Systems is known in the marketplace to have the most durable and maintenance free Towline solutions as well as the world’s fastest automated order picking technologies. The newest additions to our material handling solution portfolio are the Mobile-Matic™ XL picking robot, a completely re-engineered Simon™ Automated Guided Vehicle, a solution set of Automated Storage and Retrieval technologies, and related software enhancements to complement. The new additions were added to support a broader customer demand for flexible automation solutions and address market gaps in our existing offerings.

SI Systems’ automated material handling systems are currently used by manufacturing, assembly, order fulfillment, and distribution operations customers located primarily in North America, including the U.S. government. Our markets are diverse, and our customers and prospects represent leading manufacturer brands and their supply chain partners in the logistics services space. We sell our products directly and through integration partners.

SI Systems’ business is largely dependent upon a limited number of large contracts with a limited number of customers. This dependence can cause unexpected fluctuations in sales volume. Various external factors affect the customers’ decision-making process on expanding or upgrading their current production or distribution sites. Customers’ timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. SI Systems believes that its business is not subject to seasonality, although the rate of new orders can vary substantially from month to month. Since the Company recognizes sales on a percentage of completion basis for its systems contracts, fluctuations in SI Systems’ sales and earnings occur with increases or decreases in major installations.

### **Distribution**

Our distribution operations are carried out through our subsidiary SED International de Colombia, S.A.S. (“SED Colombia” or “SEDC”). SED Colombia currently distributes IT hardware products from 27 top worldwide leading IT manufacturers such as Hewlett Packard, Lenovo, Dell, Samsung, LG, Epson, Ricoh and others.

SEDC business is divided into three main business units: Value, Transactional and Integrated Services. The Value business unit focuses on enterprise sales and business projects, typically selling more specialized products that usually carry higher margins. The top products distributed by our Value unit include servers, workstations, storage, networking, high-end printers, high-end audio visual and power protection systems.

The SEDC Transactional business unit focuses on the consumer business (retail resellers / e-tailers) as well as run rate products for Value Added Resellers (VARs) selling to small and medium businesses (SMB). The top products distributed by the Transactional business unit include notebook computers, desktop computers, printers, TVs, audio/visual equipment, projectors, gaming and accessories.

The services provided by our Integrated Service business unit include managed services, printing outsourcing, electronic documents management, electronic invoicing and IoT. The Integrated Service unit has also taken ownership of the extended warranties and maintenance agreements sales.

## **(1) Description of Business and Summary of Significant Accounting Policies** *(Continued)*

### **Description of Business and Concentrations of Credit Risk** *(Continued)*

#### **Real Estate**

In December 2017, Ohana Home Services, LLC, a wholly owned subsidiary of Paragon, was established to acquire real estate for income and capital appreciation purposes. In December 2017, Paragon acquired residential real estate in Las Vegas, Nevada for \$750,000. In January 2018, Paragon transferred title of the real estate to Ohana. There was no consideration exchanged between the parties. In January 2018, Ohana acquired a second similar residential property also in Las Vegas, Nevada for \$750,000. Ohana intends to lease its real estate to generate positive cash flow for the foreseeable future and may seek to monetize its real estate holdings during favorable market conditions.

#### **Investments**

Paragon also invests in businesses and securities under the Investment Management Policy. The Investment Management Policy sets forth the parameters under which a portion of Paragon's cash balance may be invested in marketable securities, including U.S. Treasuries, equities of publicly traded companies, bonds, money market instruments and other securities. Investment decisions under the Investment Management Policy are made by Hesham Gad, Chairman and Chief Executive Officer. The Investment Management Policy sets forth restrictions on the investment of Paragon's funds, including an aggregate limit on Paragon's cash balance that is made available for investment, limits on the amount that may be invested in any single equity or fixed income position or certain categories of securities, prohibition of short-selling, margin trading and the use of leverage, requirements for the management of the investment account, and other Board-approval requirements.

In the three months ended March 31, 2019, the Company had one customer that accounted for over 19.6% of sales. In the three months ended March 31, 2018, the Company had one customer that accounted for 10.5% of sales.

As of March 31, 2019, one customer individually owed the Company 13.1% of trade accounts receivables and was included in the sales concentration noted above. As of March 31, 2018, no customers individually owed the Company greater than 10.0% of trade accounts receivables.

SI Systems maintains its cash and cash equivalents in a financial institution located in the United States of America. At times, cash balances may be in excess of F.D.I.C. limits. Investment balances are held in broker accounts and may be in excess of S.I.P.C. limits.

#### **Principles of Consolidation**

The consolidated financial statements include the accounts of Paragon Technologies, Inc. and its wholly owned subsidiaries SI Systems, LLC (SI Systems), Ohana Home Services, LLC (Ohana) and ARK Investments, LLC (ARK). ARK owns 80% of SED International de Colombia, S.A.S.

#### **Use of Estimates**

The preparation of the financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The judgments made in assessing the appropriateness of the estimates and assumptions utilized by management in the preparation of the financial statements are based on historical and empirical data and other factors germane to the nature of the risk being analyzed. Materially different results may occur if different assumptions or conditions were to prevail. Estimates and assumptions are mainly utilized to establish the appropriateness of the inventory reserve, warranty reserve, deferred tax valuation allowance and revenue recognition on fixed price contracts.

#### **Cash and Cash Equivalents**

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, cash on deposit, amounts invested on an overnight basis with a bank or broker/dealer and other highly liquid investments purchased with an original maturity of three months or less.

## **(1) Description of Business and Summary of Significant Accounting Policies** *(Continued)*

### **Trade Accounts Receivable and Allowance for Doubtful Accounts**

Trade accounts receivable are stated at outstanding balances, less an allowance for doubtful accounts. For SI Systems, the allowance for doubtful accounts is determined by a specific identification of individual accounts. The Company writes off receivables upon determination that no further collections are probable. For SEDC, an allowance for doubtful accounts has been established based on collection experience and an assessment of the collectability of specific accounts. The overall determination of the allowance also considers credit insurance coverage and deductibles. SEDC maintains credit insurance, which protects the Company from credit losses exceeding certain deductibles (subject to certain terms and conditions). The allowance for doubtful accounts as of March 31, 2019 and 2018 was \$91,547 and \$28,428, respectively.

### **Inventories**

For SI Systems, inventories primarily consist of materials purchased or manufactured for stock and for SEDC, inventories consist of finished goods. Inventories are stated at the lower of cost (first-in, first-out method) or net realizable value. Certain SEDC vendors allow for either return of goods within a specified period (usually 45 - 90 days) or for credits related to price protection. However, for certain other vendors and inventories, the Company is not protected from the risk of inventory loss. Therefore, in determining the net realizable value of inventories, the Company identifies slow moving or obsolete inventories that (1) are not protected by vendor agreements from risk of loss, and (2) are not eligible for return under various vendor return programs. Based upon these factors, the Company estimates the net realizable value of inventories and records any necessary adjustments as a charge to cost of sales. If inventory return privileges were discontinued in the future, or if vendors were unable to honor the provisions of certain contracts which protect SEDC from inventory losses, including price protections, the risk of loss associated with obsolete, slow moving or impaired inventories would increase.

### **Marketable Securities**

The Company adopted Accounting Standards Update ("ASU") 2016-01 on January 1, 2018. The standard primarily affects the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. The Company reclassified \$83,000 between other comprehensive income and retained earnings due to the adoption of ASU 2016-01.

The Company's debt securities portfolio is designated as available-for-sale. Securities classified as available-for-sale are those securities that the Company intends to hold for an indefinite period of time but not necessarily to maturity. Securities available-for-sale are carried at fair value. Any decision to sell a security classified as available-for-sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Company's assets and liabilities, liquidity needs, capital considerations and other similar factors. Unrealized gains and losses for debt securities are reported as increases or decreases in other comprehensive income (loss). Unrealized gains and losses for equity securities are included in earnings. Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings.

Declines in the fair value of securities below their cost that are deemed to be other-than-temporary impairments (OTTI) are reflected in earnings as realized losses. In estimating OTTI under the rules for accounting for certain debt and equity securities, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than amortized cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. In instances when a determination is made that an other-than-temporary impairment exists but the investor does not intend to sell the debt security and it is not more likely than not that it will be required to sell the debt security prior to anticipated recovery, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings.

The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

**(1) Description of Business and Summary of Significant Accounting Policies** (Continued)

**Marketable Securities** (Continued)

The Company has not recognized any other-than-temporary impairment losses for the three months ended March 31, 2019 and 2018.

The amortized cost and approximate fair value of marketable securities available-for-sale as of March 31, 2019 and December 31, 2018 are summarized as follows (*in thousands*):

	Equity Securities			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2019	\$ 145	\$ 12	\$ 45	\$ 112
December 31, 2018	137	1	58	80

  

	Debt Securities			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2019	\$ 539	\$ 3	\$ 448	\$ 94
December 31, 2018	555	2	387	170

  

	Total Marketable Securities			
	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2019	\$ 684	\$ 15	\$ 493	\$ 206
December 31, 2018	692	3	445	250

At March 31, 2019, the Company had one debt security in an unrealized loss position for less than thirty-three months and four equity securities in an unrealized loss position for less than ten months. The decline in fair value is not due to credit losses. The Company does not intend to sell these securities prior to recovery and it is more likely than not that the Company will not be required to sell these securities prior to recovery and, therefore, no securities are deemed to be other-than-temporarily impaired. Fair value accounting guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

*Level 1* — Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

## **(1) Description of Business and Summary of Significant Accounting Policies (Continued)**

### **Marketable Securities (Continued)**

*Level 2* — Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

*Level 3* — Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at March 31, 2019 and December 31, 2018, are as follows (*in thousands*):

	Total Marketable Securities			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of March 31, 2019	\$ 206	\$ 206	\$ -	\$ -
As of December 31, 2018	250	250	-	-

### **Property and Equipment**

Property and equipment acquired in business combinations are recorded at fair value; additions are recorded at cost. Property and equipment are depreciated on the straight-line method over the estimated useful lives of individual assets. The Company capitalizes costs incurred to develop commercial software products or enhancements to software products where such enhancement extends the life of the products. The ranges of lives used in determining depreciation rates for machinery and equipment and software is generally 3 - 7 years and 15 years for real estate. Maintenance and repairs are charged to operations; betterments and renewals are capitalized. Upon sale or retirement of machinery and equipment, the cost and related accumulated depreciation are removed from the accounts and the resultant gain or loss, if any, is credited or charged to earnings.

### **Leases**

The Company adopted ASU 2016-02, "Leases", and all the related amendments (collectively "ASC 842") on January 1, 2019 using a modified retrospective transition approach for all leases existing at January 1, 2019, the date of the initial application. For more information on the adoption of ASU 2016-02 refer to Note 12.

The Company leases certain office, factory and warehouse space, land, and other equipment, principally under non-cancelable operating leases.

The Company determines if an arrangement is a lease at inception of the contract. The Company's key decisions in determining whether a contract is or contains a lease include establishing whether the supplier has the ability to use other assets to fulfill its service or whether the terms of the agreement enable the Company to control the use of a dedicated asset during the contract term. In the majority of the Company's contracts where it must identify whether a lease is present, it is readily determinable that the Company controls the use of the assets and obtains substantially all of the economic benefit during the term of the contract.

**(1) Description of Business and Summary of Significant Accounting Policies** (Continued)

**Leases** (Continued)

Right-of-use (“ROU”) assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at the commencement date. The Company’s lease payments are typically fixed or contain fixed escalators. The Company has elected to not separate lease and non-lease components for all of its current lease categories and therefore, all consideration is included in the lease liabilities.

For the Company’s leases that do not include an implicit rate, the Company uses its incremental borrowing rates based on the information available at the commencement date in determining the present value of future payments. The Company’s incremental borrowing rates are based on the term of the lease, the economic environment of the lease, and the effect of collateralization.

The Company’s lease terms range from one to five years and may include options to extend the lease or terminate the lease after the initial non-cancelable term. The Company does not include options in the determination of the lease term for the majority of leases as sufficient economic factors do not exist that would compel it to continue to use the underlying asset beyond the initial non-cancelable term.

The components of lease expense are as follows (in thousands):

	Three Months Ended March 31, 2019
Lease expense:	
Operating lease cost	\$ 109
Short-term lease cost	20
Net lease expense	\$ 129

Lease assets and liabilities consist of the following (in thousands):

	Statement Line Classification	March 31, 2019
Assets:		
Operating lease assets	Right of use assets	\$1,150
Current liabilities:		
Operating lease liabilities	Operating lease liabilities	\$ 419
Non-current liabilities:		
Operating lease liabilities	Operating lease liabilities	\$ 731

Other information related to leases is as follows (in thousands):

	Three Months Ended March 31, 2019
Supplemental cash flow information:	
Net cash used for operating activities related to operating leases	\$ 108
Assets obtained in exchange for lease liabilities:	
Operating leases	\$ 1,232

**(1) Description of Business and Summary of Significant Accounting Policies** (Continued)

**Leases** (Continued)

	Three Months Ended March 31, 2019
Weighted average remaining lease terms (years):	
Operating leases	3.9
Weighted average discount rate:	
Operating leases	8.3%

Future lease payments as of March 31, 2019 are as follows (in thousands):

	Operating Leases
2019	\$ 346
2020	349
2021	280
2022	247
2023	196
Thereafter	-
Total lease payments	1,418
Less: Interest	268
Present value of lease liabilities	\$ 1,150

Rental expense, net of sublease income, for the three months ended March 31, 2018 was \$104 (in thousands).

**Intangible Assets**

As a result of the acquisition of SEDC in 2017, intangible assets of a trade name and customer relationships were recognized at fair value. The details of the intangible assets and the related amortization are shown in Note 6 to the consolidated financial statements.

**Impairment of Long-Lived Assets**

The Company reviews the recovery of the net book value of long-lived assets whenever events and circumstances indicate that the net book value of an asset may not be recoverable. In cases where undiscounted expected future cash flows are less than the net book value, an impairment loss is recognized equal to an amount by which the net book value exceeds the fair value of assets. There were no impairments noted in the three months ended March 31, 2019 or 2018.

**Foreign Currency Translation**

The financial statements of the foreign operations are measured in their local currency and then translated to U.S. dollars. All balance sheet accounts have been translated using the current rate of exchange at the balance sheet date or historical rates of exchange, as applicable. Results of operations have been translated using the average monthly exchange rates. Translation gains or losses resulting from the changes in exchange rates from year to year are accumulated in a separate component of stockholders' equity and are reported in the consolidated statements of comprehensive income (loss). Realized foreign currency transaction gains and losses are included in the accompanying consolidated statements of operations.

**(1) Description of Business and Summary of Significant Accounting Policies (Continued)**

**Revenue and Cost Recognition**

The Company adopted ASU 2014-09, "Revenue from Contracts with Customers", and all the related amendments (collectively "ASC 606") on January 1, 2018, using the full retrospective method that restates prior period financial statements presented.

The restated changes made to our consolidated opening balance sheet as January 1, 2018 due to the full retrospective method of adoption of ASC 606 are as follows:

*In thousands*

	December 31, 2017 before Restatement	Reclassification of Contract Assets	Reclassification of Contract Liabilities	December 31, 2017 After Restatement
Contract assets	\$ -	\$ 90	\$ -	\$ 90
Costs and estimated earnings in excess of billings	90	(90)	-	-
Contract Liabilities	-	-	1,119	1,119
Billings in excess of costs and estimated earnings	733	-	(733)	-
Unearned support contract revenue	386	-	(386)	-

The primary revenue sources for SI Systems are for fixed price systems contracts, sales of parts or equipment and individual support service contracts. SI recognizes revenue using the following steps:

1. Identification of the contract with a customer;
2. Identification of the performance obligations in the contract;
3. Determination of the transaction price;
4. Allocation of the transaction price to the performance obligations in the contract; and
5. Recognition of revenue when, or as, performance obligations are satisfied.

Revenue on a significant portion of SI Systems contracts is currently recognized using a cost-to-cost method based on the continuous transfer of control to the customer over time. SI transfers control for the system contracts, in two ways: (1) SI's performance creates or enhances an asset that the customer controls as the customized asset is created or enhanced for our Towline brand and (2) SI has an enforceable right to payment for both our Towline and Dispensing brands. The entire contract is the performance obligation. Typically, we would not sell the design, implementation and installation individually. In addition, the warranty would not be sold separately and it is not a service agreement. The customer would not benefit from the individual good or service on its own. There is no alternative use for the customer.

The Company accounts for system contracts on an over time basis, electing an input method of estimated costs as a measure of performance completed. The selection of the measurement of progress using estimated costs was based on a thorough consideration of alternatives of various output and input measures, including contract milestones and labor hours. However, the Company has determined that other input and output measures are not an appropriate measure of progress as they do not accurately align with the transfer of control on its customized product solutions. The selection of costs incurred as a measure of progress aligns the transfer of control to the overall production of the customized system.

## **(1) Description of Business and Summary of Significant Accounting Policies (Continued)**

### **Revenue and Cost Recognition (Continued)**

For systems contracts accounted for over time using estimated costs as a measure of performance completed, the Company relies on the estimates around the total estimated costs to complete the contract ("Estimated Costs at Completion"). Total Estimated Costs at Completion include direct labor, material and subcontracting costs. Due to the nature of the efforts required to be performed to meet the underlying performance obligation, determining Estimated Costs at Completion may be complex and subject to many variables. We have a standard and disciplined quarterly process in which management reviews the progress and performance of open contracts in order to determine the best estimate of Estimated Costs at Completion. As part of this process, management reviews information including, but not limited to, any outstanding key contract matters, progress towards completion, the project schedule, identified risks and opportunities, and the related changes in estimates of costs. The risks and opportunities include management's judgment about the ability and cost to achieve the project schedule, technical requirements, and other contract requirements. Management must make assumptions and estimates regarding labor productivity and availability, the complexity of work to be performed, the availability and cost of material, and performance by subcontractors, among other variables. Based on this analysis, any quarterly adjustment to net sales or cost of sales, and the related impact on operation income are recorded as necessary in the period they become known. When estimates of total costs to be incurred on a contract exceed estimates of total revenue to be earned, a provision for the entire loss on the contract is recorded in the period in which the loss is determined.

Payment terms for system contracts include an initial payment at the time the contract is executed, with future payments dependent upon the completion of certain contract phases or targeted milestones. In the event of contract cancellation, SI Systems is entitled to payment for all work performed through the point of cancellation. Likewise, in the event of contract cancellation prior to earning revenue equal to or greater than the initial payment, SI Systems is generally not required to refund the unused portion.

For SI's revenue for sales of parts or equipment, the contract is the customer purchase order that outlines the transaction price. The performance obligation is the shipment of the products ordered by the customer, which aligns with SI's standard sales terms that title to the goods transfer to the customer upon shipment of the items. Based on the simplified nature of these contracts, total revenue related to the sale is attributable to the satisfaction of the performance obligation, which occurs upon shipment.

SI Systems offers its Order Fulfillment customers support contracts. The support contracts cover a customer's single distribution center or warehouse where SI Systems products are installed. As part of its support contracts, SI Systems provides analysis, consultation, and technical information to the customer's personnel on matters relating to the operation of its Order Fulfillment System and related equipment and/or peripherals. For SI's revenue for individual support services, the contract is the customer purchase order that outlines the transaction price. Support contracts are prepaid and typically cover a one-year period. Revenue is recognized ratably over the course of the contract term. SI is entitled to payment regardless of what level of support is required and regardless of the outcome. The performance obligation is related to the promise to have a resource available. SI analyzed the software support percentage of cost to revenue monthly, quarterly and annually for the three years ended December 31, 2018, 2017 and 2016. SI found consistency year over year in the annual percentage of cost to revenue. There were fluctuations month to month and quarter to quarter, but that can happen depending on the customer's needs and depth of support. Therefore, due to the unpredictable fluctuations, SI determined support service (in the form of availability to the customer) is provided over the life of the contract and revenue should be recognized accordingly.

SEDC recognizes revenue from contracts with customers under ASC 606. The primary revenue source for SEDC revenue is distribution of IT hardware products.

**(1) Description of Business and Summary of Significant Accounting Policies (Continued)**

**Revenue and Cost Recognition (Continued)**

SEDC recognizes revenue using the following steps:

1. Identification of the contract with a customer;
2. Identification of the performance obligations in the contract;
3. Determination of the transaction price;
4. Allocation of the transaction price to the performance obligations in the contract; and
5. Recognition of revenue when, or as, performance obligations are satisfied.

SEDC's revenues primarily result from the sale of various technology products and services. SEDC recognizes revenue as control of products is transferred to customers, which generally happens upon shipment. Products sold by SEDC are delivered via shipment from SEDC's facilities, or by electronic delivery of keys for non-hardware products. SEDC considers customer purchase orders, which in some cases are governed by master agreements, to be the contracts with a customer. All revenue is generated from contracts with customers. The Company considers shipping as costs to fulfill the sales of products. Shipping revenue is included in net sales when control of the product is transferred to the customer, and the related shipping costs are included in cost of products sold. Shipping is not considered a separate performance obligation but is part of the product sales.

For SEDC's integrated services contracts, the performance obligation is to lease equipment and related technology (e.g., antivirus software) for a specified number of months per the contract. The customer is invoiced monthly and revenue and the related cost are recognized in the same month. Therefore, there is no contract asset or liability related to the integrated services.

Taxes imposed by governmental authorities on the Company's revenue producing activities with customers, such as value added tax, are passthrough amounts and are not recorded in the statement of operations.

The Company disaggregates our revenue from contracts with customers by geographic location, major product lines and timing of revenue recognition. See details in the tables below for the three months ended March 31, 2019 and 2018.

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

Revenue and Cost Recognition (Continued)

Disaggregation of Total Net Sales (in thousands)	Three Months Ended March 31, 2019			
	Automation	Distribution	Real Estate	Total
<b>Primary Geographical Markets</b>				
North America	\$ 1,439	\$ -	\$ 21	\$ 1,460
Latin America	2	21,963	-	21,965
Europe & Asia	275	-	-	275
<b>Total Net Sales</b>	<b>\$ 1,716</b>	<b>\$ 21,963</b>	<b>\$ 21</b>	<b>\$ 23,700</b>
<b>Major Goods/Service Lines</b>				
Material handling systems	1,060	-	-	1,060
Software support	184	-	-	184
Parts & equipment	472	-	-	472
Transactional	-	18,130	-	18,130
Value	-	3,595	-	3,595
Services	-	238	-	238
Residential real estate rental income	-	-	21	21
<b>Total Net Sales</b>	<b>\$ 1,716</b>	<b>\$ 21,963</b>	<b>\$ 21</b>	<b>\$ 23,700</b>
<b>Timing of Revenue Recognition</b>				
Goods transferred at a point in time	472	21,925	-	22,397
Goods & services transferred over time	1,244	38	21	1,303
<b>Total Net Sales</b>	<b>\$ 1,716</b>	<b>\$ 21,963</b>	<b>\$ 21</b>	<b>\$ 23,700</b>

Disaggregation of Total Net Sales (in thousands)	Three Months Ended March 31, 2018			
	Automation	Distribution	Real Estate	Total
<b>Primary Geographical Markets</b>				
North America	\$ 1,245	\$ -	\$ 15	\$ 1,260
Latin America	12	17,465	-	17,477
Europe & Asia	36	-	-	36
<b>Total Net Sales</b>	<b>\$ 1,293</b>	<b>\$ 17,465</b>	<b>\$ 15</b>	<b>\$ 18,773</b>
<b>Major Goods/Service Lines</b>				
Material handling systems	711	-	-	711
Software support	186	-	-	186
Parts & equipment	396	-	-	396
Transactional	-	13,877	-	13,877
Value	-	3,106	-	3,106
Services	-	482	-	482
Residential real estate rental income	-	-	15	15
<b>Total Net Sales</b>	<b>\$ 1,293</b>	<b>\$ 17,465</b>	<b>\$ 15</b>	<b>\$ 18,773</b>
<b>Timing of Revenue Recognition</b>				
Goods transferred at a point in time	396	17,460	-	17,856
Goods & services transferred over time	897	5	15	917
<b>Total Net Sales</b>	<b>\$ 1,293</b>	<b>\$ 17,465</b>	<b>\$ 15</b>	<b>\$ 18,773</b>

(1) **Description of Business and Summary of Significant Accounting Policies** (Continued)

**Revenue and Cost Recognition** (Continued)

Contract Balances (in thousands)

	March 31, 2019	December 31, 2018
Receivables	\$ 12,983	\$ 14,080
Contract assets	29	338
Contract liabilities	1,342	1,290

Contract assets consist of amounts formerly classified as costs and estimated earnings in excess of billings where the Company does not yet have an unconditional right to bill. Contract liabilities consist of amounts formerly classified as billings in excess of costs and estimated earnings and unearned support contract revenue.

Payment terms on system contracts are typically tied to implementation milestones associated with progress on contracts while revenue recognition is over-time based on a cost-to-cost method of measuring performance. The Company may recognize a contract asset or contract liability, depending on whether revenue has been recognized in excess of billings or billings in excess of revenue. The Company does not record a financing component to contracts when it expects, at contract inception, that the period between the transfer of a promised good or service and related payment terms are less than a year, applying practical expedients available under the accounting standards.

SI Systems records advance payments for unearned support contracts in the balance sheet as a contract liability that are in excess over amounts recognized as revenue at the end of each period. Revenue on individual support contracts is deferred and recognized on a straight-line basis over the one-year term of each individual support contract.

Revenue recognized during the three months ended March 31, 2019 and 2018 which was previously included in contract liabilities as of December 31, 2018 and 2017 is \$996 and \$472, respectively (in thousands).

There have been no impairment losses recognized on customer receivables or contract assets during the three months ended March 31, 2019 and 2018. SI Systems' contract costs include all direct material, subcontract and labor costs, and those indirect costs related to contract performance, including but not limited to costs such as indirect labor, supplies, tools, repairs, and depreciation. Selling, general and administrative costs are charged to expense as incurred.

**Product Development Costs**

The Company expenses product development costs as incurred.

**Accrued Product Warranty**

SI Systems products are warranted against defects in materials and workmanship for varying periods of time depending on customer requirements and the type of system sold, with a typical warranty period of one year. SI Systems provides an accrual for estimated future warranty costs and potential product liability claims based upon a percentage of cost of sales, typically one and one-half percent of the cost of the system being sold. A detailed review of the liability needed for products still in the warranty period is performed each quarter.

A roll-forward of warranty activities is as follows (in thousands):

	Beginning Balance January 1	Additions (Reductions) Included in Cost of Sales	Claims	Ending Balance March 31
2019.....	\$ 104	\$ -	\$ -	\$ 104
2018.....	89	12	2	103

## **(1) Description of Business and Summary of Significant Accounting Policies (Continued)**

### **Income Taxes**

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Income tax expense is the tax payable or refundable for the period, plus or minus the change during the period in deferred tax assets and liabilities.

Tax benefits for uncertain tax positions are recognized when it is more likely than not that the position will be sustained upon examination based on its technical merits. The Company classifies interest and penalties related to unrecognized tax benefits as a component of income tax expense. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision.

U.S. Tax Reform: The Tax Cuts and Jobs Act (the "Act") was enacted on December 22, 2017. The Act reduced the U.S. federal corporate tax rate from 35% to 21%, required companies to record and pay a one-time transition tax on earnings of certain foreign subsidiaries that were previously tax deferred and created new taxes on certain foreign sourced earnings.

Under the Act, a policy election with respect to the Company's treatment of potential global intangible low-tax income ("GILTI") was required to be selected for fiscal year 2018. The Company elected to account for taxes on GILTI as incurred. There was no impact to the 2018 financial statements.

SI is subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state, and local income tax examinations by tax authorities for years before 2015.

SEDC is no longer subject to income tax examinations for tax years ended before December 31, 2013. However, management and its tax advisors estimate that no significant differences may result from such contingent examinations that justify any additional accrual to cover the possibility of any expenses deemed as not allowed by the local tax authority.

### **Stock-Based Compensation**

The Company has a stock-based compensation plan in place and records the associated stock-based compensation expense over the requisite service period. Restricted stock awards that are service-based are recorded as equity and amortized into compensation expense on a straight-line basis over the vesting period. These stock-based compensation plans and related compensation expense are discussed more fully in Note 7 to the consolidated financial statements.

### **Earnings Per Share**

Basic and diluted earnings per share for the three months ended March 31, 2019 and 2018 are based on the weighted average number of shares outstanding.

## **(2) Acquisition Information**

### **SED International de Colombia S.A.S.**

On October 17, 2016, Ark Investments, LLC was formed as a wholly owned subsidiary of Paragon. On March 1, 2017, Ark Investments, LLC acquired SED International de Colombia, S.A.S. (SEDC), a Colombian based company, for a purchase price of \$1,395,000. SEDC distributes computer and technology systems in Colombia and Latin America. The Company purchased all the outstanding capital stock with cash.

**(2) Acquisition Information** (Continued)

**SED International de Colombia S.A.S.** (Continued)

SEDC was an attractive acquisition target to Paragon because of its business model and consistent earnings stream. Prior to the acquisition date, SEDC's parent company, SED International Holdings, Inc., had filed for protection under the U.S. bankruptcy regulations. The U.S. Bankruptcy Court approved bidding procedures related to the sale of SEDC in December of 2016 and then approved the purchase of SEDC by Ark Investments, LLC in February, 2017. The SEDC acquisition resulted in a bargain purchase and a gain was recorded in other income of \$4,226,089 for the year ended December 31, 2017.

Intangible assets of \$672,229 were recognized at fair value and are composed of trade name of \$536,690 and customer relationships of \$135,539.

The allocated fair value of assets acquired and liabilities assumed is summarized as follows (*in thousands*):

Cash	\$ 481
Trade accounts receivables	8,289
Inventories	9,713
Prepaid and other assets	4,176
Software and equipment	280
Deferred taxes	119
Intangible assets	672
Total assets acquired	<u>23,730</u>
Credit lines	4,798
Accounts payable	11,292
Accrued other liabilities	1,208
Income taxes payable	811
Total liabilities assumed	<u>18,109</u>
Total identified net assets acquired	5,621
Bargain purchase gain	(4,226)
	<u>\$ 1,395</u>

All acquisition related costs, including legal, professional, and other expenses, were expensed by the Company in the period incurred and not included in the purchase price. Acquisition costs were approximately \$48,000 and were included in selling, general and administrative expenses on the consolidated statement of operations for the year ended December 31, 2017.

### (3) Segment Information

Segment information for the three months ended March 31, 2019 is as follows (*in thousands*):

	Automation	Distribution	Real Estate	Investments	Eliminations	Consolidated
Net Sales to unaffiliated customers	\$ 1,716	\$ 21,963	\$ 21	\$ -	\$ -	\$ 23,700
Gross Profit	510	1,472	21	-	-	2,003
Operating income (loss)	(112)	384	(20)	-	-	252
Foreign Currency transaction gain (loss)	-	(159)	-	-	-	(159)
Interest expense, net	(15)	(112)	-	-	6	(121)
Interest income	-	8	-	2	(6)	4
Investment income	-	-	-	12	-	12
Income tax expense	(25)	123	-	-	-	98
Net income (loss) attributable to Paragon Technologies, Inc. and subsidiaries	(105)	134	(20)	14	-	23
Total assets at March 31, 2019	\$ 4,793	\$ 38,245	\$ 1,398	\$ 206	\$ (7,453)	\$ 37,189

Segment information for the three months ended March 31, 2018 is as follows (*in thousands*):

	Automation	Distribution	Real Estate	Investments	Eliminations	Consolidated
Net Sales to unaffiliated customers	\$ 1,293	\$ 17,464	\$ 16	\$ -	\$ -	\$ 18,773
Gross Profit	340	1,370	-	-	-	1,710
Operating income (loss)	(231)	314	(5)	-	-	78
Foreign Currency transaction gain (loss)	-	379	-	-	-	379
Interest expense, net	(17)	(80)	-	-	6	(91)
Interest income	-	7	-	2	(6)	3
Investment income	-	-	-	150	-	150
Income tax expense	(20)	106	-	-	-	86
Net income (loss) attributable to Paragon Technologies, Inc. and subsidiaries	(206)	90	(5)	152	-	31
Total assets at March 31, 2018	\$ 3,330	\$ 31,881	\$ 1,569	\$ 134	\$ (6,962)	\$ 29,952

### (3) Segment Information (Continued)

The domestic segments include automation/material handling, real estate and investments. The foreign segment is distribution.

### (4) Line of Credit

During 2019 and 2018, the Company had a \$750,000 line of credit facility with its principal bank to be used primarily for working capital purposes. The line of credit facility contains various non-financial covenants and is secured by all of the Company's trade accounts receivables and inventories. The availability on the line of credit was \$225,000 as of March 31, 2019. Interest on the line of credit facility is based on the "Wall Street Journal Prime Rate" plus 1.00%. The outstanding borrowings were \$525,000 as of March 31, 2019 and December 31, 2018, respectively.

During 2018 the Company had a \$945,000 line of credit facility with its marketable securities broker to be used primarily for general business purposes. The line of credit facility is secured by the available securities in the account. The availability on the line of credit was approximately \$0 as of March 31, 2019. Interest on the line of credit facility is based on the one (1) month Libor rate plus 225 bps. The outstanding borrowings were \$0 and \$26 as of March 31, 2019 and December 31, 2018 respectively.

SEDC currently maintains short term working capital lines of credit at five local banks as of March 31, 2019 and four local banks as of December 31, 2018. Below is a detail of these lines as of March 31, 2019 and December 31, 2018.

March 31, 2019			Line of credit		Borrowings		Availability	
Bank Name	Currency	Rate	in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
Davivienda	Local	IBR+4.116	1,505,000	474,047	352,648	111,077	1,152,352	362,970
Bancoldex	Local	DTF+7.60	1,150,000	362,229	1,150,000	362,229	0	0
Bancoomeva	Local	DTF+5	2,000,000	629,963	2,000,000	629,963	0	0
Bancolombia	USD	DTF+3.86	2,082,634	655,991	36,000	11,339	2,046,634	644,652
de Occidente	Local	7%	1,008,838	317,765	0	0	1,008,838	317,765
			<u>7,746,472</u>	<u>2,439,995</u>	<u>3,538,648</u>	<u>1,114,608</u>	<u>4,207,824</u>	<u>1,325,387</u>

  

December 31, 2018			Line of credit		Borrowings		Availability	
Bank Name	Currency	Rate	in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
Davivienda	Local	IBR+4.116	1,505,000	463,113	559,837	172,271	945,163	290,842
Bancoomeva	Local	DTF+5	2,000,000	615,432	2,000,000	615,432	0	0
Bancolombia	USD	DTF+2.6	2,332,502	717,748	1,177,167	362,233	1,155,335	355,515
de Occidente	Local	7%	4,543,698	1,398,169	0	0	4,543,698	1,398,169
			<u>10,381,200</u>	<u>3,194,462</u>	<u>3,737,004</u>	<u>1,149,936</u>	<u>6,644,196</u>	<u>2,044,526</u>

**(4) Line of Credit (Continued)**

SEDC also has an accounts receivable factoring credit arrangement with two local banks as of March 31, 2019 and December 31, 2018. Below is the detail of the arrangements.

March 31, 2019		AR factoring arrangement		Borrowings		Availability	
Bank Name	Rate	in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
de Occidente	7.03%	4,000,000	1,259,926	2,890,599	910,485	1,109,401	349,441
AV Villas	8.16%	5,200,000	1,637,904	5,190,805	1,635,007	9,195	2,897
		<u>9,200,000</u>	<u>2,897,830</u>	<u>8,081,404</u>	<u>2,545,492</u>	<u>1,118,596</u>	<u>352,338</u>

December 31, 2018		AR factoring arrangement		Borrowings		Availability	
Bank Name	Rate	in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
de Occidente	TBD	4,000,000	1,230,864	0	0	4,000,000	1,230,864
AV Villas	DTF+2.5	4,500,000	1,384,722	0	0	4,500,000	1,384,722
		<u>8,500,000</u>	<u>2,615,586</u>	<u>0</u>	<u>0</u>	<u>8,500,000</u>	<u>2,615,586</u>

Indicador Bancario de Referencia "IBR" and Depositos a Termino Fijo "DTF" are market reference rates in the Colombian financial market. These rates are published daily by the Banco de la Republica. The rates that are TBD have no current borrowing activity. The rates are established at time of borrowing.

SEDC also has revolving credit agreements for factoring accounts payable from HP Inc., Lenovo and Epson with three local banks as of March 31, 2019 and December 31, 2018. The factoring arrangements allow for 74 to 77 days' payment terms at 0% interest rate. If the 74 to 77 days are exceeded, interest will be charged at the prevailing market rate for the excess period.

March 31, 2019		AP factoring agreement		Borrowings		Availability	
Bank Name		in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
Bancolombia		8,500,000	2,677,342	3,545,424	1,116,743	4,954,576	1,560,599
Bancolombia Panamá		1,587,395	500,000	0	0	1,587,395	500,000
de Occidente		5,691,162	1,792,611	5,691,162	1,792,611	0	0
		<u>15,778,557</u>	<u>4,969,953</u>	<u>9,236,586</u>	<u>2,909,354</u>	<u>6,541,971</u>	<u>2,060,599</u>

December 31, 2018		AP factoring agreement		Borrowings		Availability	
Bank Name		in '000 pesos	in USD	in '000 pesos	in USD	in '000 pesos	in USD
Bancolombia		8,500,000	2,615,586	6,867,530	2,113,249	1,632,470	502,337
Bancolombia Panama		1,624,875	500,000	1,623,913	499,704	962	296
De Occidente		2,156,302	663,528	2,156,302	663,528	0	0
		<u>12,281,177</u>	<u>3,779,114</u>	<u>10,647,745</u>	<u>3,276,481</u>	<u>1,633,432</u>	<u>502,633</u>

## **(5) Uncompleted Contracts**

Costs and estimated earnings and billings on uncompleted contracts are as follows (*in thousands*):

	March 31, 2019	December 31, 2018
Costs and estimated earnings on uncompleted contracts	\$ 3,362	\$ 4,842
Less: billings to date	(4,675)	(5,794)
	<u>\$ (1,313)</u>	<u>\$ (952)</u>

Included in accompanying balance sheets under the following captions:

Contract assets	\$ 29	\$ 338
Contract liabilities	(1,342)	(1,290)
	<u>\$ (1,313)</u>	<u>\$ (952)</u>

## **(6) Intangible Assets**

Intangible assets are as follows (*in thousands*):

	March 31, 2019		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Trade name	\$ 537	\$ 112	\$ 425
Customer relations	135	28	107
	<u>\$ 672</u>	<u>\$ 140</u>	<u>\$ 532</u>
	December 31, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Trade name	\$ 537	\$ 98	\$ 439
Customer relations	135	25	110
	<u>\$ 672</u>	<u>\$ 123</u>	<u>\$ 549</u>

## **(7) Stock Options and Non-Vested Stock**

### **2012 Equity Incentive Plan**

On July 27, 2012, the Board of Directors of the Company adopted the Paragon Technologies, Inc. 2012 Equity Incentive Plan (the "Plan"). Under the Plan, the Board may grant restricted stock, stock options, stock appreciation rights and other equity-based awards to employees, directors and consultants of the Company. Initially, there were 200,000 shares of the Company's common stock available for grant under the Plan. The Plan provides that it will be administered by the Board or a committee of the Board that may be designated in the future. The Plan has a term of 10 years. On September 18, 2013, the Board of Directors increased the number of shares of common stock available for grant under the Plan to 350,000 shares.

During the three months ended March 31, 2019 and March 31, 2018, 10,000 shares were granted to an employee, respectively. Stock-based compensation expense recognized during the three months ended March 31, 2019 and 2018 for stock-based compensation programs was \$10,000 and \$11,400 for employee stock grants, respectively. All of the stock-based compensation expense was a component of selling, general and administrative expenses.

The Company estimates the fair value of stock options on the grant date by applying the Black-Scholes option pricing valuation model. The application of this valuation model involves assumptions that are highly subjective, judgmental, and sensitive in the determination of compensation cost.

## **(7) Stock Options and Non-Vested Stock (Continued)**

### **Restricted Stock – Non-controlling Interest**

The Company was party to an agreement to grant a 20% noncontrolling interest (NCI) in SEDC to El-Gibhor, an entity controlled by Mr. Ronell Rivera, President of SEDC. The acquisition date fair value of the NCI was \$209,250. The fair value of the NCI was calculated by taking 20% of the fair value of the total consideration less a 25% discount for lack of control. Total compensation expense for the year ended December 31, 2017 related to the NCI was \$209,250. As of December 31, 2017, El-Gibhor was fully vested in the 20% NCI.

### **Chairman’s Compensation and Directors’ Fees Paid**

For 2018, Mr. Gad was paid \$150,000 in cash for his roles as chairman of the board and director. The other directors were paid \$36,000 in cash in four equal quarterly installments in advance of each quarter.

For 2019, Mr. Gad as chairman and director is expected be paid the same fees as stated above for 2018. For 2019, the other directors are also expected to be paid the same fees as stated above for 2018.

As of December 2017, Mr. Gad began serving as CEO of SI Systems, LLC, a subsidiary of the Company. In that role, Mr. Gad received compensation of \$4,000 every two weeks and for the year ended December 31, 2018, his total compensation as CEO of SI Systems totaled \$104,000.

For 2019, Mr. Gad receives compensation of \$5,500 every two weeks for his role as CEO of SI Systems, LLC and for the three months ended March 31, 2019, his total compensation as CEO of SI Systems totaled \$33,000.

## **(8) Employee Benefit Plans**

The Company has a defined contribution Retirement Savings Plan (the “Savings Plan”) for its U.S. employees. Employees age 21 and above are eligible to participate in the Savings Plan. The Company matching contribution for the three months ended March 31, 2019, and 2018 was \$5,302 and \$5,269, respectively. The Savings Plan also contains provisions for profit sharing contributions in the form of cash as determined annually by the Company’s Board of Directors. There were no profit sharing contributions for the three months ended March 31, 2019, and 2018. Total expense for the Savings Plan, including Savings Plan expenses, was \$5,302 and \$5,269 for the three months ended March 31, 2019 and 2018, respectively.

## **(9) Income Taxes**

The provision for income tax expense (benefit) consists of the following (*in thousands*):

		For the Three Months Ended March 31, 2019	For the Three Months Ended March 31, 2018
Federal:	current	\$ (23)	\$ 89
	deferred	-	-
		<u>(23)</u>	<u>89</u>
State:	current	(6)	(6)
	deferred	-	-
		<u>(6)</u>	<u>(6)</u>
Foreign:	current	127	3
	deferred	-	-
		<u>127</u>	<u>3</u>
		\$ <u>98</u>	\$ <u>86</u>

## **(9) Income Taxes (Continued)**

The Company had no federal net operating losses at December 31, 2018. The Company had state net operating losses of approximately \$2,038 (in thousands) at December 31, 2018, expiring at various times based on individual state limits.

Valuation allowances are provided to reduce the carrying amount of deferred tax assets when it is more likely than not that some portion or all of the deferred tax assets will not be realized. When assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the appropriate taxing jurisdictions during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, taxable income in carryback years, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income, management has concluded that the Company's domestic deferred tax assets are more likely than not to expire before the Company can use them and, therefore, the Company's management has concluded that a full valuation allowance for deferred tax assets, net of deferred tax liabilities, was appropriate as of December 31, 2018 and 2017.

## **(10) Contingencies**

From time to time, the Company is involved in various claims and legal actions arising in the ordinary course of business. On March 27, 2017, John A. Harrell filed a lawsuit against SI Systems in the United States District Court for the District of Delaware regarding alleged breaches of a Stock Purchase Agreement between Mr. Harrell and SI Systems, dated on or about April 15, 2013. The parties settled the matter on December 28, 2017, and the case was dismissed by the Court with prejudice pursuant to the terms of that settlement on January 8, 2018. All expenses related to the settlement have been included in selling, general and administrative expenses for the year ended December 31, 2017. There are no pending actions as of March 31, 2019.

## **(11) Stock Repurchase Program**

On May 14, 2015, the Company's board of directors approved a program to repurchase up to \$250,000 of its outstanding stock. There were no stock repurchases during the three months ended March 31, 2019 and 2018.

## **(12) Recently Adopted Accounting Pronouncements**

In February 2016, the FASB issued ASU No. 2016-02, "Leases," which amends existing guidance to require lessees to recognize assets and liabilities on the balance sheet for the rights and obligations created by long-term leases and to disclose additional quantitative and qualitative information about leasing arrangements. This was subsequently amended by ASU No. 2018-01, "Land Easement Practical Expedient for Transition to Topic 842," ASU No. 2018-10, "Codification Improvements to Topic 842, Leases," and ASU No. 2018-11, "Targeted Improvements" (collectively "ASC 842"). ASC 842 establishes a ROU model that requires a lessee to recognize a ROU asset and lease liability on the balance sheet for all leases with an initial term longer than twelve months. Leases will be classified as finance or operating, with classification affecting the pattern and presentation of expense recognition in the income statement.

The Company adopted ASC 842 as of January 1, 2019 using a modified retrospective transition approach for all leases existing at January 1, 2019, the date of the initial application. Consequently, financial information will not be updated and disclosures required under ASC 842 will not be provided for dates and periods before January 1, 2019.

ASC 842 provides for a number of optional practical expedients in transition. The Company elected the practical expedients, which permit the Company to not reassess prior conclusions about lease identification, lease classification and initial direct costs under ASC 842. The Company did not elect the "use-of hindsight" practical expedient to determine the lease term or in assessing the likelihood that a lease purchase option will be exercised, allowing it to carry forward the lease term as determined prior to adoption of ASC 842.

## **(12) Recently Adopted Accounting Pronouncements (Continued)**

ASC 842 also provides practical expedients for an entity's ongoing accounting. The Company elected the short-term lease recognition exemption for all leases that qualify. A short-term lease is one with a term of 12 months or less, including any optional periods that are reasonably certain of exercise. For those leases that qualify, the exemption allows the Company to not recognize ROU assets or lease liabilities, including not recognizing ROU assets or lease liabilities for existing short-term leases at transition. Short-term lease costs are recognized as rent expense on a straight-line basis over the lease term consistent with the Company's prior accounting. The Company also elected the practical expedient to not separate lease and non-lease components for all current lease categories.

The Company recognized operating lease liabilities of \$1.15 million based on the present value of the remaining minimum rental payments determined under prior lease accounting standards and corresponding ROU assets of \$1.15 million.

For arrangements where the Company is the lessor, the adoption of ASC 842 did not have a material impact on its financial statements as the majority of its leases are operating leases embedded within managed services contracts. ASC 842 provides a practical expedient for lessors in which the lessor may elect, by class of underlying asset, to not separate non-lease components from the associated lease component and, instead, to account for these components as a single component if both of the following are met: (1) the timing and pattern of transfer of the non-lease component(s) and associated lease component are the same and (2) the lease component, if accounted for separately, would be classified as an operating lease. The accounting under the practical expedient depends on which component(s) is predominant in the contract. The Company has elected the above practical expedient and determined that the lease components are predominant and is accounting for the sublease per the guidance of ASC 842-30.

## **(13) Subsequent Events**

Events and transactions for items that should potentially be recognized or disclosed in these financial statements occurring subsequent to the balance sheet date of March 31, 2019, have been evaluated through May 15, 2019, the date which these financial statements were available to be issued.