

Argyle Security Acquisition CORP
Form 10-Q
August 14, 2006

UNITED STATES

**SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934
For the quarterly period ended June 30, 2006.**

or

**Transition Report Pursuant to Section 13 or 15(d) of the Securities
Exchange Act of 1934
For the transition period from _____ to _____.**

Commission File Number: 000-51639

Argyle Security Acquisition Corporation
(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

20-3101079
(I.R.S. Employer
Identification No.)

200 Concord Plaza, Suite 700, San Antonio, TX 78216
(Address of Principal Executive Offices including Zip Code)

(210) 828-1700
(Registrant's Telephone Number, Including Area Code)

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

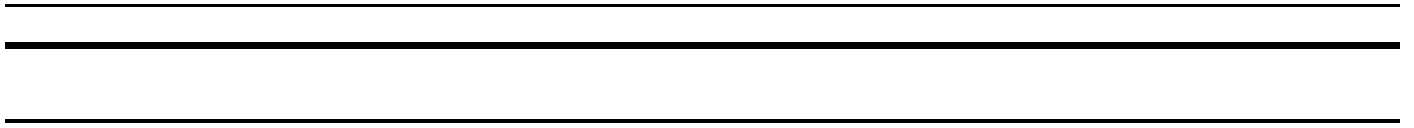
Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange. (Check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

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

There were 4,781,307 shares of the Registrant's common stock issued and outstanding as of August 11, 2006.



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ITEM 1 - FINANCIAL STATEMENTS (UNAUDITED)

Argyle Security Acquisition Corporation
(a development stage company)

Balance Sheet

| | June 30, 2006 (unaudited) | December 31, 2005 |
|---|------------------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 474,748 | \$ 9,608 |
| Cash and cash equivalents, held in trust | 29,291,422 | - |
| Prepaid expenses | 51,334 | - |
| Other assets, deferred offering costs | - | 294,745 |
| Total current assets | 29,817,504 | 304,353 |
| Property and equipment, net of accumulated depreciation of \$532 | 5,988 | - |
| Total assets | \$ 29,823,492 | \$ 304,353 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accrued expenses | \$ 118,348 | \$ 132,096 |
| Notes payable - stockholders | - | 155,000 |
| Deferred underwriting costs | 1,404,379 | - |
| Total liabilities | 1,522,727 | 287,096 |
| Common stock, subject to possible redemption - 764,627 shares at \$7.14 per share and associated deferred interest of \$113,954 | 5,573,389 | - |
| Stockholders' Equity: | | |
| Preferred stock — \$.0001 par value; 1,000,000 shares authorized; 0 shares issued and outstanding | - | - |
| Common stock—\$.0001 par value; 89,000,000 shares authorized; issued and outstanding: 4,781,307 at June 30, 2006 (including 764,627 shares of common stock subject to possible redemption) and 937,500 at December 31, 2005 | 478 | 94 |
| Additional paid-in capital | 22,765,623 | 24,906 |
| Deficit accumulated during the development stage | (38,725) | (7,743) |
| Total stockholders' equity | 22,727,376 | 17,257 |
| Total liabilities and stockholders' equity | \$ 29,823,492 | \$ 304,353 |

See notes to unaudited financial statements

Argyle Security Acquisition Corporation
(a development stage company)

Unaudited Statements of Operations

| | Three months ended June 30, 2006 | Inception through June 30, 2005 | Six months ended June 30, 2006 | Inception through June 30, 2006 |
|--|---|--|---|--|
| Operating expenses | \$ 257,743 | \$ 88 | \$ 579,449 | \$ 584,481 |
| Other income and expense | | | | |
| Bank interest income | 5,650 | - | 6,236 | 6,236 |
| Interest on cash and cash equivalents held in trust | 353,155 | - | 570,059 | 570,059 |
| Interest expense | (27,362) | - | (27,828) | (30,539) |
| Total other income and expense | 331,443 | - | 548,467 | 545,756 |
| | | | | |
| Income/(Loss) before provision for income taxes | 73,700 | (88) | (30,982) | (38,725) |
| Provision for income taxes | - | - | - | - |
| Net income/(loss) | 73,700 | (88) | (30,982) | (38,725) |
| | | | | |
| Deferred interest, attributable to common stock subject to possible redemption | 70,595 | - | 113,954 | 113,954 |
| | | | | |
| Net income/(loss) allocable to holders of non-redeemable common stock | \$ 3,105 | \$ (88) | \$ (144,936) | \$ (152,679) |
| | | | | |
| Net income/(loss) per share - - basic and diluted | \$ 0.02 | \$ (0.00) | \$ (0.01) | \$ (0.02) |
| Weighted average number of shares outstanding - - basic and diluted | 4,781,307 | 937,500 | 4,169,385 | 2,501,594 |
| | | | | |
| Net income/(loss) per share exclusive of shares and related interest subject to possible redemption - - basic and diluted | \$ 0.00 | \$ (0.00) | \$ (0.04) | \$ (0.07) |
| Weighted average number of shares outstanding exclusive of shares subject to possible redemption - - basic and diluted | 4,016,680 | 937,500 | 3,527,267 | 2,190,836 |

See notes to unaudited financial statements

Argyle Security Acquisition Corporation
(a development stage company)

Unaudited Statements of Stockholders' Equity

| | Common Stock Shares | Common Stock Amount | Paid-in Capital in Excess of Par | Deficit Accumulated During the Development Stage | Total Stockholders' Equity |
|--|------------------------|------------------------|---|--|----------------------------------|
| Stock issuance on June 23, 2005 at \$.027 | 937,500 | \$ 94 | \$ 24,906 | \$ - | \$ 25,000 |
| Net loss | | | | \$ (7,743) | (7,743) |
| Balances , at December 31, 2005 | 937,500 | \$ 94 | \$ 24,906 | \$ (7,743) | \$ 17,257 |
| Stock issuance on January 24, 2006 at \$8 | 125,000 | 12 | 999,988 | - | 1,000,000 |
| Stock issuance on January 30, 2006 at \$8 | 3,625,000 | 362 | 28,999,638 | - | 29,000,000 |
| Stock issuance on January 30, 2006 at \$8 | 75,046 | 8 | 600,360 | - | 600,368 |
| Proceeds from issuance of option to underwriters | - | - | 100 | - | 100 |
| Expenses of offerings | - | - | (2,417,117) | - | (2,417,117) |
| Less: Proceeds subject to possible redemption of 764,627 shares and associated deferred interest | - | - | (5,573,389) | - | (5,573,389) |
| Stock based compensation | - | - | 130,632 | - | 130,632 |
| Officer and director option exercise | 18,761 | 2 | 505 | - | 507 |
| Net loss | - | - | - | (30,982) | (30,982) |
| Balances , at June 30, 2006 | 4,781,307 | \$ 478 | \$ 22,765,623 | \$ (38,725) | \$ 22,727,376 |

See notes to unaudited financial statements

Argyle Security Acquisition Corporation
(a development stage company)

Unaudited Statement of Cash Flows

| | Six months ended June 30, 2006 | Inception through June 30, 2005 | Inception through June 30, 2006 |
|---|-----------------------------------|---------------------------------------|------------------------------------|
| Cash flows from operating activities | | | |
| Net loss | \$ (30,982) | \$ (88) | \$ (38,725) |
| Adjustment to reconcile net loss to net cash provided by operating activities: | | | |
| Stock based compensation | 130,632 | - | 130,632 |
| Depreciation expense | 532 | - | 532 |
| Increase in prepaid expenses | (51,334) | - | (51,334) |
| Increase in accrued expenses | 114,253 | - | 118,348 |
| Interest earned on cash and cash equivalents, held in trust | (570,059) | - | (570,059) |
| Interest expense on deferred underwriting costs | 27,362 | - | 27,362 |
| Net cash used in operating activities | (379,596) | (88) | (383,244) |
| Cash flows from investing activities: | | | |
| Purchases of investments held in trust | (178,921,809) | - | (178,921,809) |
| Maturity of investments held in trust | 150,200,446 | - | 150,200,446 |
| Purchase of property and equipment | (6,520) | - | (6,520) |
| Net cash used in investing activities | (28,727,883) | - | (28,727,883) |
| Cash flows from financing activities | | | |
| Gross proceeds from public offering and private placement | 30,600,368 | - | 30,600,368 |
| Offering costs | (873,356) | (50,000) | (1,040,100) |
| Proceeds from issuance and exercises of options | 607 | - | 607 |
| Repayment of notes payable, stockholders | (155,000) | - | (155,000) |
| Proceeds from notes payable, stockholders | - | 125,000 | 155,000 |
| Proceeds from sale of common stock to founding stockholders | - | 25,000 | 25,000 |
| Net cash provided by financing activities | 29,572,619 | 100,000 | 29,585,875 |
| Net increase in cash | 465,140 | 99,912 | 474,748 |
| Cash, beginning of period | 9,608 | - | - |
| Cash, end of period | \$ 474,748 | \$ 99,912 | \$ 474,748 |
| Supplemental disclosure of cash flow information | | | |
| Cash paid for interest | \$ 3,177 | \$ - | \$ 3,177 |
| Supplemental schedule of non-cash financing activities: | | | |
| Accrual of deferred underwriting costs | \$ 1,377,017 | \$ - | \$ 1,377,017 |

See notes to unaudited financial statements

Argyle Security Acquisition Corporation
(a development stage company)

Notes to Unaudited Financial Statements
June 30, 2006

Note 1 - Basis of Presentation

The financial statements of Argyle Security Acquisition Corporation (the "Company") as of June 30, 2006, for the three and six months ended June 30, 2006, for the period from June 22, 2005 (inception) to June 30, 2006 (cumulative) and for the period from inception to June 30, 2005, are unaudited. In the opinion of management, all normal recurring adjustments considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results to be expected for the year ending December 31, 2006.

The statements and related notes have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to such rules and regulations. These financial statements should be read in conjunction with the financial statements that were included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, as filed with the U.S. Securities and Exchange Commission.

Note 2 - Organization, business operations and summary of significant accounting policies

The Company was incorporated in Delaware on June 22, 2005 as a blank check company formed to acquire, through merger, capital stock exchange, asset acquisition or other similar business combination, a business in the security industry.

As of June 30, 2006, the Company had not completed an acquisition and was still in the development stage. All activity through June 30, 2006 relates to the Company's formation, its initial public offering and initiation of its search for a target business.

The Company completed a private placement (the "Private Placement") on January 24, 2006 and received net proceeds of approximately \$900,000. Also on January 24, 2006, the registration statement for the Company's initial public offering (the "Public Offering") was declared effective. The Company consummated the Public Offering on January 30, 2006 and received net proceeds of approximately \$27.3 million. The Company's management has broad discretion with respect to the specific application of the net proceeds of the Private Placement and the Public Offering (collectively the "Offerings"), although substantially all of the net proceeds of the Offerings are intended to be generally applied toward consummating a business combination with a target company. As used herein, a "target business" shall include an operating business in the security industry and a "business combination" shall mean the acquisition by the Company of a target business.

Of the proceeds from the Offerings, approximately \$28.7 million was deposited into a trust account ("Trust Account") until the earlier of (i) the consummation of the first business combination or (ii) the distribution of the Trust Account as described below. The amount in the Trust Account includes approximately \$1.3 million of contingent underwriting compensation and \$45,000 of contingent private placement fees which will be paid to the underwriters if a business combination is consummated, but which will be forfeited if public stockholders elect to have their shares redeemed for cash if a business combination is not consummated. The remaining proceeds may be used to pay for business, legal and accounting due diligence on prospective acquisitions and continuing general and administrative expenses.

The Company, after signing a definitive agreement for the acquisition of a target business, will submit such transaction for stockholder approval. The Company will proceed with a business combination only if a majority of the shares of common stock voted by the public stockholders are voted in favor of the business combination and public stockholders owning less than 20% of the aggregate shares sold in this offering and the private placement exercise their redemption rights. The officers and directors of the Company ("Initial Stockholders"), have agreed to vote their 937,500 founding shares of common stock in accordance with the vote of the majority in interest of all other stockholders of the Company with respect to any business combination and to vote the 125,000 shares of common stock included in the units they purchased in the Private Placement and any shares they acquire in the aftermarket in favor of the business combination. After consummation of the Company's first business combination, these voting agreements will no longer be applicable.

With respect to the first business combination which is approved and consummated, any holder of shares sold in the Public Offering, other than the Initial Stockholders and their nominees (the "Public Stockholders") who voted against the business combination may demand that the Company redeem his or her shares. The per share redemption price will equal \$7.14 per share plus interest earned thereon in the Trust Account, net of taxes payable. Public Stockholders holding 19.99% of the aggregate number of shares sold in this offering and the private placement may seek redemption of their shares in the event of a business combination. Accordingly, an amount classified as common stock subject to possible redemption and the associated deferred interest has been reflected in the accompanying balance sheet.

The Company's Certificate of Incorporation provides for liquidation of the Company in the event that the Company does not consummate a business combination within 18 months from the date of consummation of the Public Offering, or 24 months from the consummation of the Public Offering if certain extension criteria have been satisfied. The Initial Stockholders have waived their right to liquidation distributions with respect to the shares of common stock owned by them prior to the Public Offering. Accordingly, in the event of such a liquidation, the amount in the Trust Account will be distributed to the holders of the shares sold in the Public Offering.

Cash and cash equivalents

The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents.

Income taxes

Deferred income taxes are recorded based on enacted statutory rates to reflect the tax consequences in future years of the differences between the tax bases of assets and liabilities and their financial reporting amounts. Deferred tax assets, such as net operating loss carryforwards, which will generate future tax benefits are recognized to the extent that realization of such benefits through future taxable earnings or alternative tax strategies in the foreseeable short term future is more likely than not.

Recently issued accounting pronouncements

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123 (revised 2004), "Share based payment" ("SFAS 123(R)"). SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. The Company adopted SFAS 123(R) on January 1, 2006.

In June, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48), an interpretation of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (FAS 109). FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a recognition threshold for tax positions taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December

15, 2006. We are currently evaluating the impact FIN 48 will have on our financial position or results of operations.

Use of estimates

The preparation of 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 reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ from those estimates.

Note 3 - Offerings

Public Offering

On January 30, 2006, the Company sold 3,700,046 units (which includes 75,046 units sold by the underwriters pursuant to a partial exercise of their over-allotment option) to the public at a price of \$8.00 per unit. Each unit consists of one share of the Company's common stock, \$0.0001 par value, and one redeemable common stock purchase warrant ("warrant"). Each warrant entitles the holder to purchase from the Company one share of common stock at an exercise price of \$5.50 commencing the later of the completion of a business combination with a target business or January 24, 2007 and expiring January 24, 2011. The warrants are redeemable by the Company at a price of \$.01 per warrant upon 30 days notice after the warrants become exercisable, only in the event that the last sale price of the common stock is at least \$11.50 per share for any 20 trading days within a 30 trading day period ending three business days before a notice of redemption is delivered.

Private Placement

On January 24, 2006, the Company sold to certain of its officers and directors an aggregate of 125,000 units identical to the units sold in the Public Offering at a price of \$8.00 per unit.

Note 4 - Notes Payable to Stockholders

In 2005, the Company issued unsecured promissory notes to the officers of the Company totaling \$155,000. The Notes had an interest rate of 4% per annum and were paid in full with proceeds from the Public Offering, including aggregate interest of \$3,177.

Note 5 - Stockholders' Equity

On July 13, 2005 the Company granted to its officers, directors and their respective affiliates certain options, which were exercisable only in the event the underwriters exercised the over allotment option, to purchase that number of shares enabling them to maintain their 20% ownership interest without regard to the units they purchased in the private placement. The measurement date was deemed to be January 30, 2006, the date the over allotment was exercised because the number of options to be issued was not known until that date.

On January 30, 2006 the underwriters exercised the over allotment option in the amount of 75,046 units. On February 1, 2006 the officers and directors exercised their options and purchased 18,761 units for an aggregate cost of \$507. The compensation cost resulting from these share-based payments was \$130,632 at January 30, 2006 using the Black-Scholes pricing model. This model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. The fair value of the options was estimated at the measurement date using the following assumptions:

- § Weighted average volatility factor of 0.10;
- § No expected dividend payments;
- § Weighted average risk-free interest rate of 5%;
- § A weighted average expected life of 0.13 years.

The fair value of each option was \$6.99 per share. The exercise price of each option was \$0.027 per share. All options vested immediately at the measurement date and no further options may be exercised pursuant to this over-allotment provision. Compensation expense was recognized immediately and recorded as an operating expense.

As of June 30, 2006, no officer or director of the Company holds options to purchase the Company's securities.

The Company's officers and their respective affiliates purchased an aggregate of 125,000 units in the Private Placement, but have waived their right to liquidation distributions with respect to the shares of common stock included in such units. Accordingly, in the event of such a liquidation, the amount in the Trust Account will be distributed to the holders of the shares sold in the Public Offering.

The Company sold to the underwriters for \$100, options to purchase up to an aggregate of 187,500 units. The units issuable upon exercise of these options are identical to those sold on January 24, 2006. These options will be exercisable at \$8.80 per unit commencing on the later of the consummation of a business combination or one year from January 24, 2006, and expiring January 24, 2011. The options to purchase the 187,500 units and the Securities underlying such units have been deemed compensation by the National Association of Securities Dealers ("NASD") and are therefore subject to a 180-day lock-up pursuant to Rule 2710(g) (1) of the NASD Conduct Rules. Additionally, these options may not be sold, transferred, assigned, pledged or hypothecated for a one-year period (including the foregoing 180-day period) following January 24, 2006. However, these options may be transferred to any underwriter and selected dealer participating in the offering and their bona fide officers or partners.

The Company accounted for these purchase options as a cost of raising capital and included the instrument as equity in its financial statements. Accordingly, there is no net impact on the Company's financial position or results of operations, except for the recording of the \$100 proceeds from the sale. The Company has estimated, based upon a Black Scholes model, that the fair value of the purchase options on the date of sale was approximately \$3.40 per unit, (a total value of approximately \$637,500) using an expected life of five years, volatility of 44%, and a risk-free rate of 5%. However, because the Company's units do not have a trading history, the volatility assumption was based on information currently available to management. The volatility estimate was derived using historical data of public companies in the proposed industry. The Company believes the volatility estimate calculated from these companies was a reasonable benchmark to use in estimating the expected volatility of our units; however, the use of an index to estimate volatility may not necessarily be representative of the volatility of the underlying securities. Although an expected life of five years was used in the calculation, if the Company does not consummate a business combination within the prescribed time period and it liquidates, the options will become worthless.

The Company has engaged Rodman & Renshaw, LLC (the "Representative"), on a non-exclusive basis, as its agent for the solicitation of the exercise of the warrants. To the extent not inconsistent with the guidelines of the NASD and the rules and regulations of the Securities and Exchange Commission, the Company has agreed to pay the Representative for bona fide services rendered a commission equal to 5% of the exercise price, if the exercise was solicited by the Representative. In addition to soliciting, either orally or in writing, the exercise of the warrants, the Representative's services may also include disseminating information, either orally or in writing, to warrant holders about the Company or the market for the Company's securities, and assisting in the processing of the exercise of the warrants. No compensation will be paid to the Representative upon the exercise of the warrants if:

- § the market price of the underlying shares of common stock is lower than the exercise price;
- § the holder of the warrants has not confirmed in writing that the representative solicited the exercise;
- § the warrants are held in a discretionary account;
- § the warrants are exercised in an unsolicited transaction; or
- § the arrangements to pay the commission is not disclosed to warrant holders at the time of exercise.

Note 6 - Common stock reserved for issuance

As of June 30, 2006, 3,825,046 shares of common stock were reserved for issuance upon exercise of redeemable warrants and 375,000 shares of common stock were reserved for issuance pursuant to the underwriters' unit purchase option described above.

Note 7 - Preferred Stock

The Company is authorized to issue 1,000,000 shares of preferred stock with such designations, voting and other rights and preferences, as may be determined from time to time by the Board of Directors.

Note 8 - Income Taxes

The provision for income taxes for the period from January 1, 2006 through June 30, 2006 is as follows:

| | January 1, 2006 Through June 30, 2006 |
|---------------------------|---|
| Current tax expense | \$ (16,806) |
| Deferred tax benefit | 26,962 |
| Less: Valuation allowance | (10,156) |
| | \$ 0 |

The Company recorded a \$16,806 provision for its current taxable income and a valuation allowance against its net deferred tax assets in the amount of \$10,156. The valuation allowance is the result of an evaluation of the uncertainty associated with the realization of the benefit of these tax assets.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward Looking Statements

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about us that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as “may,” “should,” “could,” “would,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “continue,” or the negative of such terms or other similar expressions. Factors that might cause or contribute to such a discrepancy include, but are not limited to, those described in our other Securities and Exchange Commission filings. The following discussion should be read in conjunction with our unaudited Financial Statements and related Notes thereto included elsewhere in this report.

Critical Accounting Policies

The preparation of 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 reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ from those estimates.

Management does not believe that any recently issued, but not yet effective, accounting standards if currently adopted would have a material effect on the accompanying financial statements.

Overview

Argyle Security Acquisition Corporation is a recently organized Delaware corporation incorporated on June 22, 2005 in order to serve as a vehicle for the acquisition of an operating business through a merger, capital stock exchange, asset acquisition or other similar business combination. We intend to leverage the industry experience of our executive officers by focusing our efforts on identifying a prospective target business in the security industry. We believe that businesses involved in this industry represent attractive acquisition targets for a number of reasons, including the increase in global demand for integrated security-related products and services since September 11, 2001, the development of new technology which has the potential to expand applications and the trend towards integrated networked solutions. We are presently focusing on several potential business combinations and, during the second quarter and continuing through early August 2006, we have reviewed and/or had discussions with a number of potential target businesses regarding a possible business combination.

Results of Operations for the six-month period ended June 30, 2006

We incurred a net loss of \$30,982 for the six-month period ended June 30, 2006 before the deduction of \$113,954 of interest income attributable to common stock subject to possible redemption. We incurred a net loss of \$88 for the period from inception (June 22, 2005) through June 30, 2005.

Our trust account earned interest of \$570,059 for the six months ended June 30, 2006. Until we enter into a business combination, we will not generate operating revenues. We had no funds in trust as of June 30, 2005.

For the six months ended June 30, 2006, we incurred \$249,831 of consulting and professional fees, \$130,632 of stock compensation, \$73,991 of franchise taxes, \$36,667 of insurance expense, \$27,430 of rental expense pursuant to our lease of office space and other operating costs of \$60,898.

Results of Operations for the three-month period ended June 30, 2006

We earned net income of \$73,700 for the three-month period ended June 30, 2006 before the deduction of \$70,595 of interest income attributable to the common stock subject to possible redemption. . We incurred a net loss of \$88 for the period from inception (June 22, 2005) through June 30, 2005.

Our trust account earned interest of \$353,155 for the three months ended June 30, 2006 and our funds outside of the trust account earned interest of \$5,650.

For the three months ended June 30, 2006, we incurred \$138,159 of consulting and professional fees, \$46,042 of franchise taxes, \$22,000 of insurance expense, \$16,622 of rental expense and other operating costs of \$34,920.

Liquidity and Capital Resources

On January 24, 2006, the Company completed a private placement of 125,000 units to its executive officers and their affiliates and received net proceeds of approximately \$900,000. On January 30, 2006, we consummated our initial public offering of 3,700,046 units (which includes 75,046 units sold as part of the underwriter's over-allotment option). Each unit in both the private placement and the public offering consisted of one share of common stock and one redeemable common stock purchase warrant. Each warrant entitles the holder to purchase from us one share of our common stock at an exercise price of \$5.50 per share commencing on the later of the completion of a business combination or January 24, 2007 and expires January 24, 2011. Our common stock and warrants started trading separately as of March 2, 2006.

The net proceeds from the sale of our units, after deducting certain offering expenses of approximately \$2.4 million, including underwriting discounts of approximately \$1.8 million, were approximately \$28.2 million. Approximately \$27.3 million of the proceeds from the initial public offering and the private placement was placed in a trust account for our benefit. Except for reimbursement of taxes payable as a result of interest income earnings from the trust account and \$600,000 in interest from the trust account that may be released to us to be used as working capital, we will not be able to access the amounts held in the trust until we consummate a business combination. The \$29.3 million currently held in trust includes approximately \$1.4 million of underwriter's and placement agent's compensation from our private placement and initial public offering that will be paid to them only in the event of a business combination. The amounts held outside of the trust account are available to be used by us to provide for business, legal and accounting due diligence on prospective acquisitions and continuing general and administrative expenses. As of June 30, 2006, we had approximately \$475,000 outside the trust account to fund our working capital requirements.

We expect to use substantially all of the net proceeds of the initial public offering to acquire a target business, including identifying and evaluating prospective acquisition candidates, selecting the target business, and structuring, negotiating and consummating the business combination. To the extent that our capital stock is used in whole or in part as consideration to effect a business combination, the proceeds held in the trust account as well as any other net proceeds not expended will be used to finance the operations of the target business or, if any stockholders choose to redeem their shares, to pay such stockholders the redemption amount due to them.

Assuming the release of the full amount of interest we are entitled to receive from the trust account, we believe we will have sufficient funds outside of the trust account to operate through the next twelve months, assuming that a business combination is not consummated during that time. We do not believe we will need to raise additional funds in order to meet the expenditures required for operating our business. However, we may need to raise additional funds through a private offering of debt or equity securities if such funds are required to consummate a business

combination that is presented to us. We would only consummate such a financing simultaneously with the consummation of a business combination.

As of February 1, 2006 we entered into a lease for our office space and began to pay a base rental of approximately \$5,500 per month. The lease terminates on January 31, 2007. In connection with our operations, in March 2006, we paid an outstanding obligation to a consultant for approximately \$53,000 and are currently paying approximately \$24,000 per month in consulting fees for services assisting us in the identification of a target business and with securities compliance. The consulting agreements entered into thus far may be terminated by either party for any reason upon 15 days notice.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the sensitivity of income to changes in interest rates, foreign exchanges, commodity prices, equity prices, and other market-driven rates or prices. We are not presently engaged in and, if a suitable business target is not identified by us prior to the prescribed liquidation date of the trust fund, we may not engage in, any substantive commercial business. Accordingly, we are not and, until such time as we consummate a business combination, we will not be, exposed to risks associated with foreign exchange rates, commodity prices, equity prices or other market-driven rates or prices. The net proceeds of our initial public offering held in the trust account are to be invested only in money market funds meeting certain conditions under Rule 2a-7 promulgated under the Investment Company Act of 1940 or United States treasury bills. Given our limited risk in our exposure to money market funds and treasury bills, we do not view the interest rate risk to be significant.

ITEM 4. CONTROLS AND PROCEDURES

An evaluation of the effectiveness of our disclosure controls and procedures as of June 30, 2006 was made under the supervision and with the participation of our management, including our Co-Chief Executive Officers (one of whom serves as our principal financial officer). Based on that evaluation, our Co-Chief Executive Officers concluded that our disclosure controls and procedures are effective as of the end of the period covered by this report to ensure that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. During the most recently completed fiscal quarter, there has been no significant change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2005, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K and below are not the only risks facing our Company.

We would also like to make you aware of the following additional risk factors that holders of our securities should consider:

If we liquidate, the procedures we must follow under Delaware law are time-consuming and may result in residual liability for our stockholders

If we do not consummate a business combination by the later of July 24, 2007, or January 24, 2008 in the event that a letter of intent, an agreement in principle or a definitive agreement to complete a business combination was executed but not consummated by July 24, 2007, then, pursuant to Article SIXTH of our second amended and restated certificate of incorporation, and in accordance with Section 281(b) of the Delaware General Corporation Law, we will adopt a plan of dissolution, and as soon as reasonably possible after dissolution, make liquidating distributions to our stockholders.

Under the Delaware General Corporation Law, stockholders may be held liable for claims by third parties against a corporation to the extent of distributions received by them in a dissolution. To mitigate against this possibility, we ask our vendors and potential target businesses to waive any right, title, interest or claim of any kind in or to any monies held in the trust account. As a result of this, we believe that the claims that could be made against us are limited and the likelihood that any claim would result in any liability extending to the trust account is small. If we wind up our affairs in compliance with either Section 280 or 281(b) of the Delaware General Corporation Law following a dissolution, pursuant to Section 282 of the Delaware General Corporation Law, the potential liability of our stockholders will be limited to the lesser of the stockholder's pro-rata share of any claim or the amount distributed to the stockholder. As we do not anticipate seeking dissolution under the complex procedures of Section 280, we expect that, in accordance with Section 281(b), we will seek stockholder approval of a plan of dissolution to provide for our payment, based on facts known to us at such time, of existing and pending claims, and claims that may be potentially brought against us within the subsequent 10 years. We estimate the costs associated with the implementation and completion of such a plan of dissolution and liquidation to be approximately \$50,000 to \$75,000, which would be funded by any funds not held in our trust account and funds released to us to fund working capital.

The procedures required for us to liquidate under the Delaware General Corporation Law, or a vote to reject any plan of dissolution and distribution by our stockholders, may result in substantial delays in the liquidation of our trust account to our public stockholders as part of our plan of dissolution and distribution.

We may choose to redeem our outstanding warrants at a time that is disadvantageous to our warrant holders.

Subject to there being a current prospectus under the Securities Act of 1933, we may redeem all our outstanding warrants at any time after they become exercisable at a price of \$.01 per warrant, upon a minimum of 30 days prior written notice of redemption, if and only if, the last sale price of our common stock equals or exceeds \$11.50 per share for any 20 trading days within a 30 trading day period ending three business days before we send the notice of redemption. Calling all of our outstanding warrants for redemption could force the warrant holders:

- to exercise the warrants and pay the exercise price for such warrants at a time when it may be disadvantageous for the holders to do so,
 - to sell the warrants at the then current market price when they might otherwise wish to hold the warrants, or
- to accept the nominal redemption price which, at the time the warrants are called for redemption, is likely to be substantially less than the market value of the warrants.

Our warrant holders may not be able to exercise their warrants, which may create liability for us.

Holders of the warrants we issued in our initial public offering will be able to receive shares upon exercise of the warrants only if (i) a current registration statement under the Securities Act of 1933 relating to the shares of our common stock underlying the warrants is then effective and (ii) such shares are qualified for sale or exempt from qualification under the applicable securities laws of the states in which the various holders of warrants reside. Although we have agreed to use our best efforts to maintain a current registration statement covering the shares underlying the warrants to the extent required by federal securities laws, and we intend to comply with such agreement, we cannot assure that we will be able to do so. In addition, some states may not permit us to register the shares issuable upon exercise of our warrants for sale. The value of the warrants will be greatly reduced if a registration statement covering the shares issuable upon the exercise of the warrants is not kept current or if the securities are not qualified, or exempt from qualification, in the states in which the holders of warrants reside. Holders of warrants who reside in jurisdictions in which the shares underlying the warrants are not qualified and in which there is no exemption will be unable to exercise their warrants and would either have to sell their warrants in the open market or allow them to expire unexercised. If and when the warrants become redeemable by us, we may exercise our redemption right even if we are unable to qualify the underlying securities for sale under all applicable state securities laws. Since our obligations in this regard are subject to a “best efforts” standard, it is possible that, even if we are able to successfully assert a defense to a claim by warrant holders due to impossibility, a court may impose monetary damages on us to compensate warrant holders due to the change in circumstances that led to us being unable to fulfill our obligations.

Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or operating results.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit

| No. | Description |
|------------|---|
| 10.1(1) | Lease between the Company and Frost National Bank, Trustee For A Designated Trust |
| 31.1 | Certification of the Co-Chief Executive Officer (Principal Financial Officer) pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended |
| 31.2 | Certification of the Co-Chief Executive Officer and (Principal Executive Officer) pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended |
| 32.1 | Certification of the Co-Chief Executive Officers pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 . |
| 99.1(2) | Consulting Agreement with Alan Wachtel |
| 99.2(2) | Consulting Agreement with Mark Mellin |
| 99.3(2) | Consulting Agreement with Point Management Associates |
| (1) | Incorporated by reference to our Current Report on Form 8-K dated April 20, 2006. |
| (2) | Incorporated by reference to our Current Report on Form 8-K dated May 1, 2006. |

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ARGYLE SECURITY ACQUISITION CORPORATION

August 11, 2006

By: /s/ Bob Marbut
Bob Marbut
Co-Chief Executive Officer (Principal
Accounting and Financial officer)

By: /s/ Ron Chaimovski
Ron Chaimovski
Co-Chief Executive Officer (Principal
Executive Office)
