QUARTERLY REPORT

FOR THE PERIOD ENDED
June 30, 2012

PARAGON TECHNOLOGIES, INC.

600 Kuebler Road
Easton, PA 18040
Phone: 610-252-3205
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I.R.S. Employer Identification No.	**CUSIP No.**
22-1643428	69912T108

<u>ISSUER'S EQUITY SECURITIES</u>

COMMON STOCK

$1.00 Par Value

20,000,000 Common Shares Authorized

1,554,310 Shares Issued and Outstanding

PARAGON TECHNOLOGIES, INC.

Quarterly Report

For The Period Ended June 30, 2012

Item 1. Exact name of the issuer and the address of its principal executive offices:

The name of the issuer is Paragon Technologies, Inc. The issuer was formerly known as SI Handling Systems, Inc. until April 5, 2000.

The issuer is a Delaware corporation, incorporated on November 21, 2001. The issuer was originally incorporated in Pennsylvania on June 18, 1958. The issuer changed its state of incorporation from Pennsylvania to Delaware on November 21, 2001.

Paragon Technologies, Inc.'s contact information is as follows:

Paragon Technologies, Inc.
Attention: Hesham M. Gad, Chairman
600 Kuebler Road
Easton, PA 18040-9201
Phone: .... (610) 252-3205
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Internet: .... www.sihs.com
E-mail: .... info@sihs.com

On May 24, 2012, the Company formed a wholly-owned subsidiary, SI Systems, Inc. ("SI Systems"), a Delaware corporation. On July 1, 2012, Paragon Technologies, Inc. ("Paragon" or the "Company") contributed or transferred substantially all of its assets, properties, rights, contracts, employees, including a portion of its cash, to SI Systems, and SI Systems assumed substantially all of the liabilities and obligations of Paragon relating to or arising out of Paragon's business activities in exchange for all of the authorized shares of SI Systems' common stock; see subsequent events footnote.

Item 2. Shares outstanding:

The number of shares or total amount of the securities outstanding for each class of securities authorized is as follows:

Year-End Date	June 30, 2012	December 31, 2011	December 31, 2010
Number of shares authorized	20,000,000	20,000,000	20,000,000
Number of shares outstanding	1,554,310	1,554,310	1,554,310
Shares owned by directors and officers	383,896	515,615	435,415
Freely tradable shares *(public float)*	1,170,414	1,038,695	1,118,895
Total number of beneficial shareholders	341	354	410
Total number of shareholders of record	228	230	235

As of June 30, 2012, there were 1,554,310 shares of the Company's Common Stock issued and outstanding. As of the filing of this Quarterly Report, there were 1,554,310 shares of the Company's Common Stock issued and outstanding.

Item 3. Interim financial statements:

The Company's consolidated financial statements as of and for the period ended June 30, 2012 are incorporated by reference and can be found at the end of this Quarterly Report. The consolidated financial statements as of and for the period ended June 30, 2012 include (1) consolidated balance sheets, (2) consolidated statements of operations, (3) consolidated statements of cash flows, (4) consolidated statements of stockholders' equity, and (5) notes to consolidated financial statements.

Item 4. Management's discussion and analysis or plan of operation:

The Company's Management Discussion and Analysis for the period ended June 30, 2012 is attached and is incorporated herein by reference.

Item 5. Legal proceedings:

None for the period ended June 30, 2012 and through the date of this report.

Item 6. Default upon senior securities:

None for the period ended June 30, 2012 and through the date of this report.

Item 7. Other information:

Not applicable.

Item 8. Exhibits:

None for the period ended June 30, 2012 and through the date of this report.

Item 9. Certifications:

I, James D. Floyd, Interim Chief Financial Officer of the issuer, certify that:

a. I have reviewed this Quarterly Report of Paragon Technologies, Inc.

b. 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

c. Based on my knowledge, the consolidated financial statements, 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.

July 30, 2012

/s/ James D. Floyd
James D. Floyd
Interim Chief Financial Officer

I, William J. Casey, Acting Chief Executive Officer of the issuer, certify that:

a. I have reviewed this Quarterly Report of Paragon Technologies, Inc.

b. 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

c. Based on my knowledge, the consolidated financial statements, 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.

July 30, 2012

/s/ William J. Casey
William J. Casey
Acting Chief Executive Officer

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Financial Statements
Paragon Technologies, Inc. and Subsidiary
Consolidated Balance Sheets (Unaudited)
June 30, 2012 and December 31, 2011
(In Thousands, Except Share and Per Share Data)

	June 30, 2012	December 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	$ 4,945	4,871
Receivables:		
Trade accounts	515	838
Other receivables	13	15
Total receivables	528	853
Costs and estimated earnings in excess of billings	677	237
Inventories:		
Raw materials	157	160
Work-in-process	2	123
Finished goods	412	294
Total inventories	571	577
Prepaid expenses and other current assets	160	101
Total current assets	6,881	6,639
Machinery and equipment, at cost:		
Machinery and equipment	1,217	1,208
Less: accumulated depreciation	1,118	1,096
Net machinery and equipment	99	112
Total assets	$ 6,980	6,751

See accompanying notes to consolidated financial statements.

(Continued)

Consolidated Financial Statements *(Continued)*
Paragon Technologies, Inc. and Subsidiary
Consolidated Balance Sheets (Unaudited)
June 30, 2012 and December 31, 2011
(In Thousands, Except Share and Per Share Data)

	June 30, 2012	December 31, 2011
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 1,181	698
Billings in excess of costs and estimated earnings	414	387
Accrued salaries, wages, and commissions	82	110
Accrued product warranties	107	76
Unearned support contract revenue	237	276
Accrued other liabilities	89	130
Total current liabilities	2,110	1,677
Commitments and contingencies *(See Notes 5 and 11)*		
Stockholders' equity:		
Common stock, $1 par value; authorized 20,000,000 shares; issued and outstanding 1,554,310 shares as of June 30, 2012 and December 31, 2011	1,554	1,554
Additional paid-in capital	3,281	3,281
Retained earnings	35	239
Total stockholders' equity	4,870	5,074
Total liabilities and stockholders' equity	$ 6,980	6,751

See accompanying notes to consolidated financial statements.

Consolidated Financial Statements *(Continued)*
Paragon Technologies, Inc. and Subsidiary
Consolidated Statements of Operations (Unaudited)
For the Six Months Ended June 30, 2012 and 2011
(In Thousands, Except Share and Per Share Data)

	Three Months Ended		Six Months Ended	
	June 30, 2012	June 30, 2011	June 30, 2012	June 30, 2011
Net sales	$ 2,447	2,425	4,443	4,723
Cost of sales	1,881	1,591	3,410	3,170
Gross profit on sales	566	834	1,033	1,553
Operating expenses:				
Selling, general and administrative expenses	586	694	1,186	1,334
Product development costs	40	5	56	21
Total operating expenses	626	699	1,242	1,355
Operating income (loss)	(60)	135	(209)	198
Other income (expense):				
Interest income	6	11	13	23
Interest expense	-	(5)	-	(1)
Other expense, net	6	(1)	(6)	(9)
Total other income (expense), net	12	5	7	13
Income (loss) before income taxes	(48)	140	(202)	211
Income tax expense	1	1	2	2
Net income (loss)	$ (49)	139	(204)	209
Basic and diluted earnings (loss) per share	$ (.03)	.09	(.13)	.13
Weighted average basic and diluted shares outstanding	1,554,310	1,554,310	1,554,310	1,554,310

See accompanying notes to consolidated financial statements.

Consolidated Financial Statements *(Continued)*
Paragon Technologies, Inc. and Subsidiary
Statements of Cash Flows (Unaudited)
For the Six Months Ended June 30, 2012 and 2011
(In Thousands)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Cash flows from operating activities:		
Net income (loss)	$ (204)	209
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:		
Depreciation of machinery and equipment	25	30
Change in operating assets and liabilities:		
Receivables	325	918
Costs and estimated earnings in excess of billings	(440)	(280)
Inventories	6	(18)
Prepaid expenses and other current assets	(59)	(95)
Accounts payable	483	16
Billings in excess of costs and estimated earnings	27	(825)
Accrued salaries, wages, and commissions	(28)	(27)
Accrued product warranties	31	13
Unearned support contract revenue	(39)	(71)
Accrued other liabilities	(41)	(2)
Net cash provided (used) by operating activities	86	(132)
Cash flows from investing activities:		
Proceeds from the disposition of machinery and equipment	-	1
Purchases of machinery and equipment	(12)	(2)
Net cash used by investing activities	(12)	(1)
Increase (decrease) in cash and cash equivalents	74	(133)
Cash and cash equivalents, beginning of year	4,871	4,892
Cash and cash equivalents, end of period	$ 4,945	4,759
Supplemental disclosures of cash flow information:		
Cash paid (received) during the period for:		
Interest expense	$ -	1
Income taxes	$ 16	20

See accompanying notes to consolidated financial statements.

<u>Consolidated Financial Statements</u> *(Continued)*
Paragon Technologies, Inc. and Subsidiary
Consolidated Statements of Stockholders' Equity ***(Unaudited)***
For the Six Months Ended June 30, 2012 and 2011
(In Thousands, Except Share Data)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Total Stockholders' Equity
	Shares	Amount			
Balance at December 31, 2010	1,554,310	$ 1,554	3,281	48	4,883
Net income	-	-	-	209	209
Balance at June 30, 2011	1,554,310	$ 1,554	3,281	257	5,092
Balance at December 31, 2011	1,554,310	$ 1,554	3,281	239	5,074
Net loss	-	-	-	(204)	(204)
Balance at June 30, 2012	1,554,310	$ 1,554	3,281	35	4,870

See accompanying notes to consolidated financial statements.

(1) <u>Basis of Financial Statement Presentation</u>

In the opinion of the management of Paragon Technologies, Inc. ("Paragon" or the "Company"), the unaudited interim consolidated financial statements furnished reflect all adjustments and accruals that are necessary to present a fair statement of results for the interim periods. Results for interim periods are not necessarily indicative of results expected for the full fiscal year.

This Quarterly Report should be read in conjunction with, and is qualified in its entirety by reference to, the Financial Statements of the Company and the related Notes thereto appearing in the Company's Annual Report for the year ended December 31, 2011 as filed with the OTC Markets Group Inc. on March 14, 2012. Refer to the Company's Annual Report for the year ended December 31, 2011 for more complete financial information.

Use of Estimates

The preparation of the consolidated 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 consolidated 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 consolidated 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, and revenue recognition on fixed price contracts.

Principles of Consolidation

The consolidated financial statements include the accounts of Paragon Technologies, Inc. and SI Systems, Inc., a wholly-owned subsidiary, after elimination of intercompany balances and transactions.

(2) <u>Business Operations</u>

Company Overview

Paragon, based out of Easton, Pennsylvania, provides a variety of material handling solutions, including systems, technologies, products, and services for material flow applications through its wholly-owned subsidiary, SI Systems, Inc. ("SI Systems"). On May 24, 2012, the Company formed a wholly-owned subsidiary, "SI Systems", a Delaware corporation. On July 1, 2012, Paragon Technologies, Inc. ("Paragon" or the "Company") contributed or transferred substantially all of its assets, properties, rights, contracts, employees, including a portion of its cash, to SI Systems, and SI Systems assumed substantially all of the liabilities and obligations of Paragon relating to or arising out of Paragon's business activities in exchange for all of the authorized shares of SI Systems' common stock; see subsequent events footnote. SI Systems' capabilities include horizontal transportation, rapid dispensing, order fulfillment, computer software, sortation, integrating conveyors and conveyor systems, and aftermarket services. Paragon is a Delaware corporation, incorporated on November 21, 2001. Paragon was originally incorporated in Pennsylvania on June 18, 1958. Paragon changed its state of incorporation from Pennsylvania to Delaware on November 21, 2001.

(2) Business Operations *(Continued)*

Company Overview *(Continued)*

SI Systems is a specialized systems integrator supplying SI Systems' branded automated material handling systems to manufacturing, assembly, order fulfillment, and distribution operations customers located primarily in North America, including the U.S. government. SI Systems' branded products are utilized to automate the movement or selection of products and are often integrated with other automated equipment such as conveyors and robots. SI Systems is brought to market as two individual brands — SI Systems' Order Fulfillment Systems (hereafter referred to as "SI Systems OFS") and SI Systems' Production & Assembly Systems (hereafter referred to as "SI Systems PAS").

SI Systems OFS focuses on providing order fulfillment systems to order processing and distribution operations, which may incorporate SI Systems' proprietary DISPENSIMATIC®, Mighty MAC® (Mobile A-Frame Cart), and automated order fulfillment solutions and specialized software from the SINTHESIS® Software Suite. SINTHESIS® is comprised of eight proprietary software groups, with 26 extendible software modules that continually assess real-time needs and deploy solutions to accurately facilitate and optimize planning, warehousing, inventory, routing, and order fulfillment within the distribution process.

SI Systems PAS focuses on providing automated material handling systems to manufacturing and assembly operations and the U.S. government, which may incorporate SI Systems' LO-TOW®, CARTRAC®, and SImon™ horizontal transportation technologies.

SI Systems' automated material handling systems are designed as labor-saving devices to improve productivity, quality, and reduce costs. SI Systems' integrated material handling solutions involve both standard and specially designed components and include integration of non-proprietary automated handling technologies to provide turnkey solutions for its customers' unique material handling needs. SI Systems' engineering staff develops and designs computer control programs required for the efficient operation of the systems and for optimizing manufacturing, assembly, and fulfillment operations.

The Company's 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. The customers' timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. The Company 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 the Company's sales and earnings occur with increases or decreases in major installations. The Company maintains its cash and cash equivalents in financial institutions located in the United States. At times, cash balances may be in excess of F.D.I.C. limits.

(3) Accrued Product Warranties

The Company's 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. The Company 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 June 30
2012	$ 76	32	(1)	107
2011	$ 71	26	(13)	84

(4) Line of Credit

On February 19, 2009, the Company established a $5,000,000 line of credit facility with its principal bank to be used primarily for working capital purposes. On December 1, 2010, the amount of the line of credit facility was reduced to $3,500,000. Interest on the line of credit facility is at the LIBOR Market Index Rate plus 1.25%. As of June 30, 2012 and December 31, 2011, the Company did not have any borrowings under the line of credit facility; however, the leasing agreement associated with the Company's principal office is secured with a $200,000 letter of credit at both June 30, 2012 and December 31, 2011 under the line of credit facility. Therefore, as of June 30, 2012 and December 31, 2011, the amount available under the line of credit was $3,300,000. There were no borrowings outstanding during the three and six months ended June 30, 2012 and during the year ended December 31, 2011.

The line of credit facility contains various non-financial covenants and is secured by all of the Company's accounts receivables and inventory. The Company was in compliance with all covenants as of June 30, 2012. The line of credit expires on November 30, 2012.

(5) Lease Commitment

The Company leases 22,700 square feet in Easton, Pennsylvania for use as its principal office. The leasing agreement requires fixed monthly rental payments of $18,000. The terms of the lease also require the payment of a proportionate share of the facility's operating expenses. The leasing agreement is secured with a $200,000 letter of credit. The lease expires on February 20, 2013.

(6) Stock Repurchase

There were no stock repurchases effected by the company during the three and six months ended June 30, 2012.

(7) Revenue and Cost Recognition

Revenues on fixed price systems contracts are recorded on the basis of the Company's estimates of the percentage of completion of individual contracts. Revenue and gross profit is recognized on the basis of the ratio of aggregate costs incurred to date to the most recent estimate of total costs. As contracts may extend over one or more years, revisions in cost and profit estimates during the course of the work are reflected in the accounting periods in which the facts requiring revisions become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is accrued.

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. Changes in job performance, job conditions, and estimated profitability may result in revisions to costs and income, which are recognized in the period in which the revisions are determined.

The asset, “Costs and estimated earnings in excess of billings,” represents revenues recognized in excess of amounts billed on uncompleted contracts. The liability, “Billings in excess of costs and estimated earnings,” represents billings in excess of revenues recognized on uncompleted contracts.

Revenues on other sales of parts or equipment are recognized when title transfers pursuant to shipping terms. There are no installation or customer acceptance aspects of these sales.

Revenue on individual support contracts is recognized on a straight-line basis over the one-year term of each individual support contract.

(8) Unearned Support Contract Revenue

The Company offers its Order Fulfillment customers one-year support contracts for an annual service fee. The support contracts cover a customer’s single distribution center or warehouse where the Company’s products are installed. As part of its support contracts, the Company 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.

The Company records advance payments for unearned support contracts in the balance sheet as a current 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.

(9) Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB authoritative guidance that addresses all forms of share-based payment awards, including shares issued under employee stock purchase plans, stock options, restricted and nonvested stock, and stock appreciation rights. It requires companies to recognize in the statement of operations the grant-date fair value of stock options and other equity-based compensation issued to employees.

(9) Stock-Based Compensation *(Continued)*

The expense associated with stock-based compensation arrangements is a non-cash charge. In the Statements of Cash Flows, stock-based compensation expense would be an adjustment to reconcile net income (loss) to net cash provided (used) by operating activities.

1997 Equity Compensation Plan
The Company's stock-based compensation program, the 1997 Equity Compensation Plan ("ECP"), expired in July 2007. Prior to expiration, the ECP provided for grants of stock options, restricted and nonvested stock, and stock appreciation rights to selected employees, key advisors who performed valuable services, and directors of the Company. In addition, the ECP provided for grants of performance units to selected employees and key advisors. Prior to expiration, the ECP, as amended by stockholders in August 2000 and June 2001, authorized up to 1,012,500 shares of common stock for issuance pursuant to the terms of the plan. No further grants are available under the plan.

Under the Company's ECP, officers, directors, and employees have been granted options to purchase shares of common stock at the market price at the date of grant. Options vest in four equal annual installments beginning on the first anniversary of the date of grant; thus, at the end of four years, the stock options are fully exercisable. Vested stock option awards may be exercised through payment of cash, exchange of mature shares, or through a broker. As of June 30, 2012, 5,000 stock options are outstanding under the plan, and all stock options have a term of seven years and expire on March 8, 2013. The exercise price of the stock options outstanding under the plan is $10.01.

There was no stock-based compensation expense recognized during the three and six months ended June 30, 2012 and 2011 and during the year ended December 31, 2011 for stock-based compensation programs.

Stock Options
There were no stock options exercised, forfeited, or granted during the three and six months ended June 30, 2012 and 2011 and during the year ended December 31, 2011.

Nonvested Stock
There are no nonvested stock awards outstanding as of June 30, 2012 and 2011.

(10) 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.

(10)Income Taxes *(Continued)*

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.

The Company has federal net operating losses of approximately $890,000 at December 31, 2011, expiring at various times through December 31, 2031. The Company has state net operating losses of approximately $2,700,000 at December 31, 2011, expiring of 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 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 June 30, 2012 and December 31, 2011.

The valuation allowance of $712,000 as of June 30, 2012 was an offset of net deferred tax assets primarily related to inventory, warranty, net operating loss carryforwards, and other temporary differences.

The valuation allowance of $639,000 as of December 31, 2011 was an offset of net deferred tax assets primarily related to inventory, warranty, net operating loss carryforwards, and other temporary differences.

As of June 30, 2012 and December 31, 2011, there were no unrecognized tax benefits.

For the three and six months ended June 30, 2012 and 2011, there was no expense related to interest and penalties, net of federal benefit, recognized in the statements of operations.

The Company recognized income tax expense during the three months ended June 30, 2012 and 2011 of $1,000 and $1,000, respectively. Income tax expense for the three months ended June 30, 2012 and 2011 was primarily related to accruals for state income tax matters. There was no income tax benefit recognized for the loss for the three months ended June 30, 2012 and 2011 as a result of the valuation allowance offsetting deferred tax assets.

(10)<u>Income Taxes</u> *(Continued)*

The Company recognized income tax expense during the six months ended June 30, 2012 and 2011 of $2,000 and $2,000, respectively. Income tax expense for the six months ended June 30, 2012 and 2011 was primarily related to accruals for state income tax matters. There was no income tax benefit recognized for the loss for the six months ended June 30, 2012 and 2011 as a result of the valuation allowance offsetting deferred tax assets.

The Company is subject to U.S. federal income tax as well as income tax of multiple state and foreign jurisdictions. The Company has substantially concluded all U.S. federal income tax matters for years through 2005. The Company files tax returns in approximately 30 state taxing jurisdictions. The Company has substantially concluded state income tax matters for years through 2003.

(11)<u>Legal Proceedings</u>

From time to time, the Company is involved in various claims and legal actions arising in the ordinary course of business. Although the amount of any liability that could arise with respect to currently pending actions cannot be accurately predicted, in the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations, or liquidity.

(12)<u>Subsequent Events</u>

Events and transactions for items that should potentially be recognized or disclosed in these financial statements occurring subsequent to the balance sheet date of June 30, 2012 have been evaluated through July 27, 2012, the date which these financial statements were available to be issued.

<u>Creation of wholly owned operating subsidiary SI Systems, Inc.</u>

On July 1, 2012, the company created a wholly owned operating subsidiary SI Systems, Inc. by contributing certain assets, properties, rights and assumed liabilities of the company’s PAS and OFS lines of business into the new subsidiary.

<u>2012 Equity Incentive Plan; Director Equity Compensation Plan</u>

On July 27, 2012, the Board of Directors of the Company adopted the Paragon Technologies, Inc. 2012 Equity Incentive 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 are 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.

Commencing with the second half of 2012, Jack H. Jacobs and Samuel S. Weiser, directors of the Company, have agreed to be paid their retainer fees in shares of the Company’s common stock. The shares of common stock will be paid to the directors quarterly in advance and will be valued based on the average of the closing bid and asked prices on the OTC Markets for the 30 trading days immediately preceding July 1, 2012. The directors will continue to be paid meeting fees in cash. This Director Equity Compensation Plan will continue in 2013 unless amended by the Board. The Board plans to review the Company’s Director Compensation Program for 2013 prior to the end of 2012.

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

The following discussion and analysis of the Company's financial condition and results of operations should be read in conjunction with the unaudited consolidated financial statements and related notes thereto included in this Quarterly Report for the period ended June 30, 2012, and the cautionary statements and financial statements and related notes thereto included in the Company's Annual Report for the year ended December 31, 2011. The discussion and analysis contains "forward-looking statements" based on management's current expectations, assumptions, estimates, and projections. These forward-looking statements involve risks and uncertainties. The Company's actual results could differ materially from those included in these "forward-looking statements" as a result of risks and uncertainties identified in connection with those forward-looking statements, including those factors identified herein, and in the Company's other publicly filed reports.

Business Overview

Paragon Technologies, Inc. provides a variety of material handling solutions, including systems, technologies, products, and services for material flow applications through its wholly-owned subsidiary, SI Systems, Inc. Founded in 1958, the Company's material handling solutions are based on core technologies in horizontal transportation and order fulfillment and are aimed at improving productivity for manufacturing, assembly, and distribution center operations.

Results of Operations – Six Months Ended June 30, 2012 Compared to the Six Months Ended June 30, 2011

Earnings Summary

The Company had a net loss of $204,000 (or $0.13 basic loss per share) for the six months ended June 30, 2012, compared to net income of $209,000 (or $0.13 basic earnings per share) for the six months ended June 30, 2011. The decrease in net income was primarily due to a decrease during the first half of 2012 in sales and gross profit of $280,000 and $520,000, respectively. Partially offsetting the decrease in net income was a decrease in selling, general and administrative expenses of $148,000 as described below.

Net Sales and Gross Profit on Sales

	2012	2011
Net sales	$ 4,443,000	4,723,000
Cost of sales	3,410,000	3,170,000
Gross profit on sales	$ 1,033,000	1,553,000
Gross profit as a percentage of sales	23.3%	32.9%

The decrease in sales was associated with a smaller backlog of orders entering 2012 when compared to the backlog of orders entering 2011.

Gross profit, as a percentage of sales, for the six months ended June 30, 2012, when compared to the six months ended June 30, 2011, was unfavorably impacted by 11.5% due to product mix, and favorably impacted by 1.9% due to the increased absorption of overhead costs.

Selling, General and Administrative Expenses

Selling, general and administrative expenses of $1,186,000 were lower by $148,000 for the six months ended June 30, 2012 than for the six months ended June 30, 2011. The favorable variance in selling, general and administrative expenses was primarily attributable to a decrease of $137,000 in legal, auditing and other professional fees.

Results of Operations – Six Months Ended June 30, 2012 Compared to the Six Months Ended June 30, 2011 *(Continued)*

Product Development Costs

Product development costs, including patent expense, of $56,000 were higher by $35,000 for the six months ended June 30, 2012 than for the six months ended June 30, 2011. Development programs in the six months ended June 30, 2012 and 2011 were primarily aimed at improvements to the Company's Order Fulfillment systems technologies. Order Fulfillment development efforts during the six months ended June 30, 2012 and 2011 included DISPENSIMATIC® hardware modifications and enhancements aimed at promoting workplace efficiencies for the Company's customers.

Interest Income

Interest income of $13,000 was lower by $10,000 for the six months ended June 30, 2012 than for the six months ended June 30, 2011. The decrease in interest income was attributable primarily to the reduced level of interest rates earned on funds available for investment.

Income Tax Expense

The Company recognized income tax expense during the six months ended June 30, 2012 and 2011 of $2,000 and $2,000, respectively. Income tax expense for the six months ended June 30, 2012 and 2011 was primarily related to accruals for state income tax matters. There was no income tax benefit recognized for the loss for the six months ended June 30, 2012 and 2011 as a result of the valuation allowance offsetting deferred tax assets.

Results of Operations – Three Months Ended June 30, 2012 Compared to the Three Months Ended June 30, 2011

Earnings Summary

The Company had a net loss of $49,000 (or $0.03 basic loss per share) for the three months ended June 30, 2012, compared to net income of $139,000 (or $0.09 basic earnings per share) for the three months ended June 30, 2011. The decrease in net income was primarily due to a decrease during the second quarter of 2012 in gross profit of $268,000. Partially offsetting the decrease in net income was a decrease in selling, general and administrative expenses of $108,000 as described below.

Net Sales and Gross Profit on Sales

	2012	2011
Net sales	$ 2,447,000	2,425,000
Cost of sales	1,881,000	1,591,000
Gross profit on sales	$ 566,000	834,000
Gross profit as a percentage of sales	23.1%	34.4%

The decrease in sales was associated with a smaller backlog of orders entering 2012 when compared to the backlog of orders entering 2011.

Gross profit, as a percentage of sales, for the three months ended June 30, 2012, when compared to the three months ended June 30, 2011, was unfavorably impacted by 13.5% due to product mix, and favorably impacted by 2.2% due to the increased absorption of overhead costs.

Results of Operations – Three Months Ended June 30, 2012 Compared to the Three Months Ended June 30, 2011 *(Continued)*

Selling, General and Administrative Expenses

Selling, general and administrative expenses of $586,000 were lower by $108,000 for the three months ended June 30, 2012 than for the three months ended June 30, 2011. The favorable variance in selling, general and administrative expenses was primarily attributable to a decrease of $148,000 in legal, auditing, other professional fees, and liability insurances, partially offset by an increase of $40,000 in sales salaries.

Product Development Costs

Product development costs, including patent expense, of $40,000 were higher by $35,000 for the three months ended June 30, 2012 than for the three months ended June 30, 2011. Development programs in the three months ended June 30, 2012 and 2011 were primarily aimed at improvements to the Company's Order Fulfillment systems technologies. Order Fulfillment development efforts during the three months ended June 30, 2012 and 2011 included DISPENSIMATIC® hardware modifications and enhancements aimed at promoting workplace efficiencies for the Company's customers.

Interest Income

Interest income of $6,000 was lower by $5,000 for the three months ended June 30, 2012 than for the three months ended June 30, 2011. The decrease in interest income was attributable primarily to the reduced level of interest rates earned on funds available for investment.

Income Tax Expense

The Company recognized income tax expense during the three months ended June 30, 2012 and 2011 of $1,000 and $1,000, respectively. Income tax expense for the three months ended June 30, 2012 and 2011 was primarily related to accruals for state income tax matters. There was no income tax benefit recognized for the loss for the three months ended June 30, 2012 and 2011 as a result of the valuation allowance offsetting deferred tax assets.

Liquidity and Capital Resources

The Company's cash and cash equivalents at June 30, 2012 were $4,945,000, representing 70.8% of total assets, compared to $4,871,000, or 72.2% of total assets, at December 31, 2011. The increase in cash and cash equivalents was primarily due to cash provided by operating activities totaling $86,000, partially offset by purchases of capital equipment totaling $12,000.

Cash provided by operating activities totaling $86,000 during the six months ended June 30, 2012 was primarily due to the following factors:

- an increase in accounts payable in the amount of $483,000 associated with the purchase of goods and services rendered in accordance with job completion requirements;
- a decrease in receivables in the amount of $325,000 in accordance with contractual requirements; and
- an increase in customers' deposits and billings in excess of costs and estimated earnings in the amount of $27,000 in accordance with contractual requirements.

Liquidity and Capital Resources *(Continued)*

Partially offset by the following factors:

- a decrease in costs and estimated earnings in excess of billings in the amount of $440,000 in accordance with contractual requirements;
- a net loss in the amount of $204,000 for the first half of 2012;
- an increase in prepaid expenses and other current assets in the amount of $59,000 primarily associated with the payment of insurance premiums for the current year; and
- an increase in accrued product warranties in the amount of $41,000 primarily associated with the establishment of warranties for contracts entering the warranty period.

The Company's cash and cash equivalents at June 30, 2011 were $4,759,000, representing 69.0% of total assets, compared to $4,892,000, or 64.5% of total assets, at December 31, 2010. The decrease was due to cash used by operating activities totaling $132,000.

Cash used by operating activities totaling $132,000 during the six months ended June 30, 2011 was primarily due to the following factors:

- an increase in costs and estimated earnings in excess of billings in the amount of $280,000 in accordance with contractual requirements;
- a decrease in customers' deposits and billings in excess of costs and estimated earnings in the amount of $825,000 in accordance with contractual requirements;
- an increase in prepaid expenses and other current assets in the amount of $95,000 primarily associated with the payment of insurance premiums for the current year; and
- a decrease in unearned support contract revenue in the amount of $71,000 relating to the recognition of revenue on support contracts on the straight-line basis.

Partially offset by the following factors:

- a decrease in receivables in the amount of $918,000 in accordance with contractual requirements;
- net income in the amount of $209,000 for the first half of 2011; and
- an increase in accounts payable in the amount of $16,000 associated with the purchase of goods and services rendered in accordance with job completion requirements.

There were no stock repurchases during the six months ended June 30, 2012 and June 30, 2011.

On February 19, 2009, the Company established a $5,000,000 line of credit facility with its principal bank to be used primarily for working capital purposes. On December 1, 2010, the amount of the line of credit facility was reduced to $3,500,000. Interest on the line of credit facility is at the LIBOR Market Index Rate plus 1.25%. As of June 30, 2012 and December 31, 2011, the Company did not have any borrowings under the line of credit facility; however, the leasing agreement associated with the Company's principal office is secured with a $200,000 letter of credit at both June 30, 2012 and December 31, 2011 under the line of credit facility. Therefore, as of June 30, 2012 and December 31, 2011, the amount available under the line of credit was $3,300,000. There were no borrowings outstanding during the three and six months ended June 30, 2012 and during the year ended December 31, 2011.

Liquidity and Capital Resources *(Continued)*

The line of credit facility contains various non-financial covenants and is secured by all of the Company's accounts receivables and inventory. The Company was in compliance with all covenants as of June 30, 2012. The line of credit facility expires on November 30, 2012.

The Company does not have any material commitments for capital expenditures as of June 30, 2012.

The Company anticipates that its financial resources, consisting of cash and cash equivalents, will be adequate to satisfy its future cash requirements through the next year. Sales volume, as well as cash liquidity, may experience fluctuations due to the unpredictability of future contract sales and the dependence upon a limited number of large contracts with a limited number of customers. Various external factors affect the customers' decision-making process on expanding or upgrading their current production or distribution sites. The customers' timing and placement of new orders is often affected by factors such as the current economy, current interest rates, and future expectations. The Company 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 the Company's sales and earnings occur with increases or decreases in major installations.

Contractual Obligations

The Company leases 22,700 square feet in Easton, Pennsylvania for use as its principal office. The leasing agreement requires fixed monthly rental payments of $18,000. The terms of the lease also require the payment of a proportionate share of the facility's operating expenses. The leasing agreement is secured with a $200,000 letter of credit. The lease expires on February 20, 2013.

Future contractual obligations and commercial commitments at June 30, 2012 as noted above are as follows:

		Payments Due by Period					
	Total	2012	2013	2014	2015	2016	After 2016
Contractual obligations:							
Operating leases	$ 144,000	108,000	36,000	-	-	-	-

	Total Amounts Committed	Amount of Commitment Expiration Per Period					
		2012	2013	2014	2015	2016	After 2016
Other commercial commitments:							
Letters of credit	$ 200,000	-	200,000	-	-	-	-

Severance

On May 2, 2012, the Board of Directors of the Company terminated the Company's Severance Pay for Executives Policy and the Severance Pay for Office Employees Policy. The Company will consider the payment of severance and other benefits upon the termination of employment of executives and other employees on a case-by-case basis, taking into account the financial circumstances of the Company and the relevant circumstances of any employee being terminated.

Employee Pay Cuts; Profit-Sharing Plan

During the quarterly period ended June 30, 2012, the Company implemented a 15% pay cut for the Company's executive officers and a 10% pay cut for substantially all other employees of the Company.

On June 1, 2012, the Company implemented a profit-sharing plan for 2012 that applies to all employees of the Company. Under the plan, the Company will pay 10% of its net income for 2012 to the Company's employees, other than commission-based sales employees and executive officers, which will be paid in equal amounts to the eligible employees. The profit-sharing payments will be made to employees who remain employed by the Company or its subsidiary through the end of 2012.

Effective as of July 16, 2012, Mr. Casey's base salary was further reduced to $95,000 per year, and Mr. Casey was provided the opportunity to earn 10% of the Company's net income for 2012 up to a maximum payment of $100,000.

Investment Management Policy

On June 29, 2012, the Company's Board of Directors approved an Investment Management Policy, which sets forth the parameters under which a portion of the Company'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. Initially, $1.0 million of the Company's cash balance is available for investment under the Investment Management Policy. The Investment Management Policy sets forth restrictions on the investment of these funds, including 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 without Board approval, requirements for the management of the investment account, and other Board-approval requirements.

Off-Balance Sheet Arrangements

As of June 30, 2012 and December 31, 2011, the leasing agreement associated with the Company's principal office is secured with a $200,000 letter of credit under the Company's line of credit. As of June 30, 2012, the Company had no other off-balance sheet arrangements in the nature of guarantee contracts, retained or contingent interests in assets transferred to unconsolidated entities (or similar arrangements serving as credit, liquidity, or market risk support to unconsolidated entities for any such assets), obligations (including contingent obligations) under a contract that would be accounted for as a derivative instrument, or obligations (including contingent obligations) arising out of variable interests in unconsolidated entities providing financing, liquidity, market risk, or credit risk support to the Company, or that engage in leasing, hedging, or research and development services with the Company.

Cautionary Statement

Certain statements contained herein are not based on historical fact and are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and the Securities and Exchange Commission rules, regulations, and releases. The Company intends that such forward-looking statements be subject to the safe harbors created thereby. Among other things, the forward-looking statements regard the Company's earnings, liquidity, financial condition, and other matters. Words or phrases denoting the anticipated results of future events, such as "anticipate," "does not anticipate," "should help to," "believe," "estimate," "is positioned," "expects," "may," "will," "will likely," "is expected to," "will continue," "should," "project," and similar expressions that denote uncertainty, are intended to identify such forward-looking statements. The Company's actual results, performance, or achievements could differ materially from the results expressed in, or implied by, such "forward-looking statements": (1) as a result of risks and uncertainties identified in connection with those forward-looking statements, including those factors identified herein, and in the Company's other publicly filed reports; (2) as a result of factors over which the Company has no control, including the strength of domestic and foreign economies, sales growth, competition, and certain costs increases; or (3) if the factors on which the Company's conclusions are based do not conform to the Company's expectations.

Quantitative and Qualitative Disclosures About Market Risk

The Company does not believe that its exposures to interest rate risk or foreign currency exchange risk, risks from commodity prices, equity prices, and other market changes that affect market risk sensitive instruments are material to its results of operations.