

**IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA**

PAUL I. BURMAN, *et. al.*)
Plaintiffs,)
v.)
PHOENIX WORLDWIDE,)
INDUSTRIES, INC., *et. al.*)
Defendants.)
Case No. 1:04CV1276
The Hon. Reggie Walton

SECOND AMENDED COMPLAINT

Plaintiffs, PAUL I. BURMAN (hereinafter “Burman”), ROBERT C.WARRINER (“Warriner”), SYLVIA J. ROLINSKI (“Rolinski”), and INGERSOLL & BLOCH, Chartered Employees Profit Sharing Plan and Trust, by and through its trustees William B. Ingersoll and Stuart Marshall Bloch (“I&B”, collectively with Burman, Warriner and Rolinski , “Plaintiffs”), by and through undersigned counsel, and pursuant to F.R.Civ.P. 7, 8, 9 and 15 and this Court’s Order entered August 30, 2005 bring this Second Amended Complaint against Defendants PHOENIX WORLDWIDE INDUSTRIES, INC. (“Phoenix”), DR. J. AL ESQUIVEL SHULER (“Shuler,” collectively with Phoenix the “Phoenix Defendants”), and the accounting firm of RACHLIN, COHEN & HOLTZ, LLP (“R&C,” collectively with the Phoenix Defendants, the “Defendants”) for statutory securities fraud, common law fraud and

misrepresentation, negligent misrepresentation, breach of fiduciary duty and negligence, and state and aver as follows:¹

INTRODUCTION

This case arises out of the misrepresentations – both express and by omission – made by the Phoenix Defendants to induce the Plaintiffs to invest in Phoenix. The Phoenix Defendants then reiterated the misrepresentations, failed to correct the misrepresentations, and failed to correct the omissions, in order to induce some of the Plaintiffs to invest additional sums in Phoenix.

Plaintiffs' Phoenix investment decisions were not the result of their lack of diligence, or of misunderstanding. To the contrary, Plaintiffs repeatedly sought from the Phoenix Defendants specific answers to material questions. Given the opportunity to correct or explain their misstatements, the Phoenix Defendants again chose outright and actionable deception.

As a direct and foreseeable consequence of the Phoenix misconduct, and the concomitant negligence of R&C, Plaintiffs were wrongly induced to invest \$1,116,500 in Phoenix.

PARTIES

Plaintiffs

1. Plaintiff Burman is an individual residing in the State of Maryland, who does, engages in and transacts business in the District of Columbia, including business out of which these claims arise. Plaintiff Burman is 87 years old. Between September 25, 2001

¹ Plaintiffs preserve for purposes of appeal certain “allegations of failure to secure revenue.” See Order at .31 and see First Amended Complaint, Count IV (Breach of Fiduciary Duty) at paragraphs 129-132, and the last clause of paragraph 133. Those claims were dismissed. Order, at 31.

and September 1, 2002, Plaintiff Burman purchased 61,400 shares of Phoenix for \$307,000.

2. Plaintiff Warriner is an individual residing in the State of Maryland, who does, engages in and transacts business in the District of Columbia, including business out of which these claims arise. On August 27, 2002, Plaintiff Warriner purchased 5,000 shares of Phoenix for \$25,000.

3. Plaintiff Rolinski is an individual residing in the State of Maryland. Between February 20, 2002 and January 15, 2003, Plaintiff Rolinski purchased 4,900 shares of Phoenix for \$34,400.

4. Plaintiff I&B is an employee profit sharing plan and trust located in the District of Columbia and doing business in the District of Columbia, including business out of which these claims arise. Jay Zawatsky ("Zawatsky") is an investment manager of I&B. William B. Ingersoll and Stuart Marshall Bloch are the trustees of I&B. Between May 28, 2002 and July 22, 2002, Plaintiff I&B purchased 150,000 shares of Phoenix for \$750,000.

In addition, on or about July 22, 2002, Trust Communities, Inc., of which Zawatsky is the president, loaned to Phoenix in a secured transaction the sum of \$2,000,000. Phoenix defaulted on that debt, and Trust Communities, Inc. accelerated the note evidencing the debt and initiated foreclosure proceedings in Miami, Florida. Subsequent thereto, Phoenix refinanced and satisfied the Trust Communities, Inc. loan.

Defendants

5. Defendant Phoenix is a corporation that has its principal place of business in the State of Florida. Phoenix solicited investments in the District of Columbia and

elsewhere. Phoenix manufactures and distributes, among other products and services, electronic systems for use in counter-terrorism and drug interdiction.

6. Defendant Shuler is an individual who, upon information and belief, resides in the State of Florida. Shuler is the founder of Phoenix . Shuler is, and at all times pertinent to the allegations in the Second Amended Complaint was, the president, chief executive officer, chairman of the board of directors, and majority stockholder of Phoenix. As of August 1, 2001, Shuler owned 76.88% of the outstanding stock of Phoenix. At the conclusion of the offering through which Plaintiffs invested, Shuler owned in excess of 60% of the outstanding shares of Phoenix. Shuler made material misrepresentations individually and on behalf of Phoenix to the Plaintiffs in the District of Columbia and elsewhere. In addition, Shuler, individually and on behalf of Phoenix, omitted to state facts that were material to the decisions of the Plaintiffs to participate in the offering of Phoenix securities.

Shuler was, and explicitly held himself out to be, privy to all material confidential and proprietary information concerning Phoenix, its operations, finances, financial condition, and present and future business prospects. Because of his possession of such information, Defendant Shuler knew of and recklessly disregarded the material misrepresentations made to Plaintiffs in connection with Plaintiffs' purchase of Phoenix securities and that material facts, which would have influenced the decisions of Plaintiffs to participate in the offering of Phoenix securities, were omitted from the securities offering materials and oral presentations to the Plaintiffs.

Defendant Shuler is liable as a direct participant in the wrongs complained of herein. In addition, Shuler, by reason of his status as chief executive officer and

chairman of the board of directors, is a “controlling person” within the meaning of Section 20 of the Exchange Act and had the power and influence to cause Phoenix to engage in the unlawful conduct complained of herein. Because of his position of control, the individual Defendant was able to and did directly, or indirectly, control the conduct of Phoenix and its agents. To the extent that Shuler personally performed that wrongful act, he is directly liable. To the extent that other persons - for whose action Shuler, as a controllingg person is liable – perfomed the wrongful act, Shuler is liable as a controlling person.

Defendant Shuler controls the Phoenix Board of Directors by virtue of his offices, his equity holdings, and his personal or family relationships with the majority of the members of the Board of Directors.

Defendant Shuler is an insider of Phoenix and is an unsecured creditor of Phoenix. At all times pertinent to the allegations of the Second Amended Complaint, Shuler was owed, or claims to have been owed by Phoenix, accrued salary or benefits of no less than \$432,000 as of August 2001. That obligation was carried on Phoenix’s books at an annual salary of \$144,000. As of March 31, 2003, according to Phoenix, “there are accruals of “\$1,008,000 and \$992,000” for “2003 and 2002” due to Shuler from Phoenix.

7. Defendant R&C is a public accounting firm that, upon information and belief, has its principal place of business in Miami, Florida. R&C prepared the audited financial statements of Phoenix. The audited financial statements were presented to and relied upon by the Defendants in Washington, D.C. and elsewhere.

R&C held itself out to Plaintiffs as an agent of Phoenix. Phoenix identified R&C as its accounting firm and agent.

Agency Relationships

8. Defendant Shuler, by virtue of his positions, offices and statements as described in paragraph 6 above, is and at all times pertinent to the allegations of the Second Amended Complaint was an agent for Phoenix.

9. Defendant R&C, by virtue of the relationship and the statements described in paragraph 7 above, is and at all times pertinent to the allegations of the Second Amended Complaint was an agent for Phoenix for accounting matters.

10. Charles Levy ("Levy") is, and at all times pertinent to the allegations of the Second Amended Complaint was, both a director and shareholder of Phoenix. Over the same period, Levy was and is the Chairman of Phoenix's Finance Committee. Levy was held out by the Phoenix Defendants as the Phoenix spokesperson, agent and representative for purchase and sale of Phoenix securities. Levy, by virtue of the offices and the statements described in this paragraph, is, and at all times pertinent to the allegations of the Second Amended Complaint was, the agent for Phoenix on matters related to the purchase and sale of Phoenix securities.

JURISDICTION

Subject Matter Jurisdiction

11. This Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. §§ 1331, 1337, and Section 27 of the Securities and Exchange Act. Further, this action arises under Sections 10(b) and 20(a) of the Securities and Exchange Act (15 U.S.C. §§ 78j(6) and 78t(a)), Rule 10b-5 promulgated thereunder (17 C.F.R. § 240.10b-

5). In connection with the acts and omissions alleged in this Complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, mails and interstate telephone and Internet communications.

12. This Court has supplemental jurisdiction pursuant to 28 U.S.C. §1367. In addition, this court has jurisdiction pursuant to 28 U.S.C. § 1332. The amount in controversy as to each Plaintiff exceeds \$75,000, exclusive of interest and costs.

Personal Jurisdiction

13. Defendants have significant personal contacts with the District of Columbia in accordance with the District of Columbia Long Arm Statute, including, but not limited to, D.C. Code § 13-423 (a) (1), (2), (3), (4). Therefore, the Defendants are subject to the personal jurisdiction of this Court. The causes of action asserted herein arise largely from Defendants' activities within the District of Columbia.

VENUE

14. Venue is proper in this Court pursuant to 28 U.S.C. § 1391(b).

FACTS COMMON TO ALL COUNTS

15 . Plaintiffs adopt and incorporate herein by reference as if specifically set forth herein the averments of paragraphs one through fourteen of the Second Amended Complaint.

16. As is more fully set forth below, the Phoenix Defendants, from August 2001 through January 2003, consistently, repeatedly, knowingly and falsely, represented to Plaintiffs orally and in writing that Phoenix had obtained specific, large scale and enforceable contracts for the sale of Phoenix products (the “Contract

Misrepresentations"). Phoenix failed to correct the Contract Misrepresentations before purchase by Plaintiffs of Phoenix securities.

17. As is more fully set forth below, the Phoenix Defendants, from August 2001 to April, 2004, knowingly and with intent to deceive, failed to disclose to Plaintiffs that Phoenix had been, and continued to be, subject to substantial Internal Revenue Service ("IRS") tax deficiencies (the "IRS Misrepresentations"). Thereafter, Phoenix failed to correct the IRS Misrepresentations, and, when affirmatively questioned by Plaintiffs on the existence of any IRS tax deficiencies, falsely denied the existence of IRS tax deficiencies.

18. As is more fully set forth below, Plaintiffs and each of them relied on the Contract Misrepresentations, and relied on the IRS Misrepresentations, for purposes of electing to purchase Phoenix securities, and that reliance was reasonable under all of the facts and circumstances. As a direct and foreseeable consequence thereof, Plaintiffs sustained monetary damage in the amount of the sums paid for purchase of the securities, as set forth below and in paragraphs one through four of the Second Amended Complaint.

As is more fully set forth below, defendant R&C failed to satisfy the applicable standard of care with regard to identification and disclosure of the IRS tax deficiencies.

Phoenix in 2001

19. In 2001 Shuler, Shuler's wife, Shuler's brother, and Levy were members of the board of directors and constituted a majority of the board.

20. On August 1, 2001, Phoenix issued a Private Placement Offering Memorandum (the "PPM") to sell 2,000,000 shares of Phoenix common stock. The

stock was to be offered to "accredited investors," pursuant to Regulation D, 17 C.F.R. § 230.501(a), Rule 501(a) promulgated pursuant to the 1933 Act.

21. The PPM represented, *inter alia*, as follows: Phoenix sought investment of ten million dollars, at \$5.00 per share; by 2001 Phoenix had recovered from the effects of Hurricane Andrew; sales productivity was hampered by lack of working capital; with appropriate investment, Phoenix would experience "exponential growth;" and proceeds from the sale of \$10,000,000 of securities would be used for "new office and showroom setup, marketing investment, demo vehicles and platforms, production equipment and upgrades, debt repayment, and working capital."

22. Phoenix needed and sought immediate and substantial capital infusions. In 2001, Phoenix was in arrears and in default on approximately \$2.6 million in debt to First Union Bank. Defendant Shuler was a personal guarantor on the First Union debt. The First Union debt carried with it restrictive covenants which limited Phoenix's ability to, among other things, secure additional financing. As a further consequence, Phoenix's ability to obtain purchase orders and to manage and finance day-to-day proposals and orders for their products was limited.

23. The Phoenix Fiscal Year ends on March 31. In the Fiscal Year ending March 31, 2001, Phoenix reported less than \$1 million in gross revenue.

The Initial Contacts

24. In August 2001, Burman was approached by an investment advisor named George Schwelling ("Schwelling"). Schwelling told Burman of an opportunity to invest in Phoenix. Prior to his conversation with Schwelling, Burman had never heard of Phoenix. Plaintiff Warriner was first informed of Phoenix by Burman.

25. In May, 2002, Zawatsky was also told by Schwelling of an opportunity to invest in Phoenix. Prior to that conversation, Zawatsky had never heard of Phoenix.

26. Rolinski was contacted by Charles Levy in 2001. Levy and Rolinski were long time acquaintances and had worked together before on other investment deals and projects. In 2001, Levy advised Rolinski of the opportunity to invest in Phoenix. Prior to that discussion, Rolinski had never heard of Phoenix.

27. In May, 2002, Zawatsky was contacted by Phoenix agent and representative Levy.

The Solicitation Period

28. From September 2001 through January 2003 (the "Solicitation Period"), the Phoenix Defendants, through Levy, solicited Plaintiffs to purchase Phoenix securities.

29. During the Solicitation Period, Levy engaged in over forty telephone conversations with Burman, over one hundred telephone conversations with Rolinski, and over sixty telephone conversations with Zawatsky. Those telephone conversations related to the purchase and the sale of Phoenix securities. Typically, Zawatsky spoke to Levy from Zawatsky's offices in the District of Columbia. Typically, Rolinski spoke to Levy from her offices in Maryland. Typically, Burman spoke to Levy from his office in Washington, D.C. Typically, when Zawatsky, Rolinski and Burman successfully placed calls to Levy, the calls would be made to North Carolina or Florida.

30. During the Solicitation Period, Levy advised Plaintiffs that each share would be sold for five dollars (\$5.00), except that, on August 27th, 2002, Shuler, in an investor update letter, advised shareholders that the price per share would rise to ten dollars (\$10.00) as of September 2, 2002. During the Solicitation Period, Levy represented that

Phoenix intended to “go public” by January 2004, and he stated that shares would be sold in a public offering at between \$20 and \$100 per share.

31. Levy, on behalf of Phoenix, during the Solicitation Period, made the following statements, in addition to the Contract Misrepresentations and the IRS Misrepresentations, to Plaintiffs about Phoenix’ capabilities and activities: Phoenix had representatives who testified before Congress, sat on a “top secret” homeland security committee, and were actively setting policy within the U.S. government concerning security issues; Phoenix possessed a “secret” manufacturing plant across the Interstate from its main facility which was being used to produce “top secret” security items for the U.S. Government and other foreign governments; Phoenix was already in production of seven different types of sensors which had the capabilities to “hear”, “see” and “smell” in order to locate and identify targets and to focus laser beams on a target to enable Predator Drone Planes to destroy such targets; these sensors were already in use by the Department of Defense in Afghanistan and that one such target was Osama Bin Laden, who may have been cornered in a cave in Tora Bora; Phoenix’s profit margins were in excess of 35% on all government contracts; Phoenix’s immediate and near term share value would increase from \$5 a share to between \$20 and \$40 a share; Shuler is the key individual in Phoenix; Phoenix maintains a \$10,000,000 life insurance policy on Shuler for the benefit of Phoenix; no material decision regarding Phoenix was ever made without Shuler’s consent, knowledge or direction.

The Contract Misrepresentations

32. In Addendum E to the August 1, 2001 PPM, Phoenix claimed the following *risk adjusted* gross revenue for three years.

Year 1 -- \$388,313,910;

Year 2 -- \$599,655,509; and

Year 3 -- \$695,145,567, totaling \$2,885,087,858 for the three years. A true and accurate copy of Addendum E is annexed to the Second Amended Complaint as *Exhibit 1* and is adopted and incorporated herein by reference as if specifically set forth herein.

33. Addendum E specifically and explicitly adjusted and analyzed Phoenix's scheduled gross income pursuant to a delineated risk assessment applied to a set of identified product sales ranging from a high of 100% to a low of 5%.

34. In Year 1: \$9,000,000 was risk adjusted at 100%; \$189,029,044 was risk adjusted at 80%; \$31,086,000 was risk adjusted at 90%; \$82,700,207 was risk adjusted at 10%; and, \$76,498,659 was risk adjusted at 5%.

35. In Year 2: \$13,000,000 was risk adjusted at 100%; \$212,657,675 was risk adjusted at 90%; \$14,250,000 was risk adjusted at 95%; \$206,750,517 was risk adjusted at 25%; and \$152,997,318 was risk adjusted at 10%.

36. In Year 3: \$17,000,000 was risk adjusted at 100%; \$372,150,930 was risk adjusted at 45%; and \$305,994,636 was risk adjusted at 20%.

37. A total of \$39,000,000 in gross revenue was, according to Phoenix's representations in Addendum E, a 100% certainty for Years 1 through 3; an additional total of \$14,500,000 was a 95% certainty in Year 2; an additional \$243,743,675 was a 90% certainty in Years 1 and 2; and, an additional \$189,029,044 was an 80% certainty in Year 1. *See Exhibit 1.*

38. On September 3, 2001, Phoenix prepared a written statement (the "September 2001 Contracts Statement") which purported to set out in color-coded format various

“Contracts in Progress.” A true and accurate color copy of the September 2001 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein. A black and white copy is annexed hereto as Exhibit 2 for convenience. The September 2001 Contracts Statement identified 21 contracts.

39. Of those contracts, 7 were highlighted in blue, 9 were highlighted in yellow, and 5 were highlighted in green. The legend on the September 2001 Contracts Statement provided as follows: Blue – “Signed Contracts;” Yellow – “Contracts in Process of being Signed;” Green – “Contracts Pending.”

The I&B and Rolinski Transactions

40. In February of 2002, Levy represented by telephone, to Rolinski in Maryland, that Phoenix had procured a contract (the “Border Contract”) with the then Immigration and Naturalization Service, now the U.S. Citizenship and Immigration Services of the Department of Homeland Security, to install sensors along the southern border of the United States. Levy further stated that “Phoenix was already providing thousands of sensors to the INS” (the “Border Contract Misrepresentation”). Relying on the Border Contract Misrepresentation, Rolinski purchased 2,000 shares of Phoenix stock, at \$5.00 per share, on February 20, 2002.

41. The Border Contract Misrepresentation was material to Rolinski’s decision to invest in Phoenix, and the truth would have assumed actual significance in Rolinski’s decision to invest in Phoenix. Rolinski would not have invested in Phoenix but for the Border Contract Misrepresentation.

42. The Border Contract Misrepresentation was false when made. The allegation of falsity is based upon Shuler's written statement, on December 6, 2002, ten months after the making of the Border Contract Misrepresentation, that: "*PWI is in final negotiations* to supply our sensors to assist in the monitoring of the southern and northern borders of the United States."(emphasis added). This statement by Shuler contradicts Levy's representation that the border contract was "executed and Phoenix was providing thousands of sensors to the INS" as of February 2002. The allegation of falsity is also based on Phoenix's actual gross revenue in Fiscal Years 1, 2 and 3, *see* para. 52 below, as well as the absence by Phoenix counsel of any assertion of the Border Contract, *see* para. 53 below, as well as the failure of the Phoenix Defendants, or their counsel, to produce at any time to Rolinski or to any other Plaintiff documentary support for the existence of the Border Contract, or for the existence of the Border Contract in February 2002, or for receipt of proceeds for the sale of sensors by Phoenix to the INS or its successor agency.

43. On May 15, 2002, Phoenix prepared a written statement (the "May 2002 Contracts Statement") that purported to be an update of the September 2001 Contracts Statement. The May 2002 Contracts Statement was again color-coded in blue, yellow and green, and contained a legend identical to the legend in the September 2001 Contracts Statement. A true and accurate copy of the May 2002 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein.

44. The May 2002 Contracts Statement identified 33 contracts. Of those contracts, 12 were highlighted in blue, 16 were highlighted in yellow, and 5 were

highlighted in green. Blue highlighted contracts on the May 2002 Contracts Statement totaled \$31,075,521.

45. A copy of the May 2002 Contracts Statement was delivered to Rolinski by Levy by way of an instrumentality of interstate commerce in June 2002.

46. Zawatsky spoke by telephone with Levy in the middle of May 2002. Several days later, on or about May 20, 2002, Zawatsky received from Levy and from Phoenix, via an instrumentality of interstate commerce, at Zawatsky's office in Washington DC, the following documents, among others: the PPM, Addendum E, the September 2001 Contracts Statement, and the May 2002 Contracts Statement.

47. Within one week of receipt of those documents, Zawatsky, from his office in Washington, DC, spoke by telephone with Levy to obtain information about Phoenix and the documents. That conversation took place subsequent to May 15, 2002 and prior to May 28, 2002.

48. Levy told Zawatsky in that conversation, that the two Contracts Statements were "updates to the Addendum E financial projections," and that the blue line items on the color-coded sheets were reflective of the 100% risk adjusted revenue items in Addendum E.

49. In that conversation, Levy also told Zawatsky that the blue line items on the May 2002 Contract Statement are "done deals" with a 100% probability of performance. When probed further by Zawatsky in that conversation, Levy said that the blue line contracts are performing and generating revenue. Levy also represented in that conversation that the line items designated in yellow were drafted and out for signature. Levy said that as soon as a yellow contract was signed, Phoenix would begin to ship the

product and get paid on the contract. Levy explained that the items designated in green were pending and under negotiation at the moment. Zawatsky asked Levy that, if all of the items in both yellow and green were ignored and one just concentrated on the items in blue, would that be the minimum amount of sales revenue Phoenix was assured to generate over the next three years. Levy replied: "absolutely."(along with the Contract Statements, and Addendum E, the "Blue Contract Misrepresentations"). The Blue Contract Misrepresentations were false.

50. In that conversation, Zawatsky asked about the exit strategy for the investment. Levy replied that Phoenix expected that Phoenix would go public by January of 2004, thereby giving investors a viable exit strategy (the "Public Sale Statements"). Levy added that, in the interim, investors would receive dividends approximately equal to their \$5.00 per share investment as a result of the cash flow generated by the blue line contracts. Levy stated that dividends would commence as early as December 2002 (the "Dividend Statements").

51. Based upon the Blue Contract Misrepresentations, as well as the Public Sale Statements and the Dividend Statements, Zawatsky, on behalf of I&B, purchased 25,000 shares of Phoenix common stock at \$5.00 per share on May 28, 2002. The Blue Contract Misrepresentations, as well as the Public Sale Statements and the Dividend Statements were material to I&B's decision to invest in Phoenix, and the truth would have assumed actual significance in I&B's decision to invest in Phoenix. Had Levy and Phoenix not made the Blue Contract Misrepresentations, I&B would not have invested in Phoenix.

52. The allegations of falsity of the Blue Contract Misrepresentations are based on the amounts of revenue reflected on each of Phoenix's audited financial statements.

During this three year period, i.e., Fiscal Years ending March 31, 2002, March 31, 2003, and March 31, 2004, Phoenix actually received only approximately one three hundredth (1/300th) of the revenue set out in Addendum E to the PPM. Phoenix reported in audited financial statements actual revenue from all sources of: Fiscal Year 2002 -- \$929,606; and Fiscal Year 2003 -- \$2,965,064. The unaudited monthly cash flow statements for Fiscal Year 2004 reflect \$5,160,155 in sales revenue. The actual revenues of \$9,034,825, therefore, were more than 75% below the \$ 39,000,000 in revenues that Phoenix had stated in Addendum E that Phoenix was 100% certain to receive in this period.

53. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, Phoenix has failed, when confronted with the possibility of this lawsuit, to produce any of the contracts claimed in the Blue Contract Misrepresentations. Further, in the Phoenix Defendants' own Motion to Dismiss the Complaint, they appear to assert only the existence of a “\$10 million dollar US Department of Defense contract for delivery of sensors.” *Memorandum*, at 11, n.2. They make no claim of any kind of any other “blue” contract.

54. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, in the supplement to the Phoenix PPM appended to an August 12, 2002, investor update letter, Shuler wrote that Phoenix was “awaiting orders for proposed projects” from Venezuela. However, the May 2002 Contracts Statement identifies that item as a “blue” contract. In that same supplement, Phoenix wrote that it was “awaiting orders” for two Saudi Arabian contracts, notwithstanding that, in the May 2002 Contracts Statement, the Saudi Arabia items were identified as a “blue” contract and as a “yellow” contract.

55. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, at a meeting of the Phoenix Board of Directors, after the Plaintiffs had made the vast bulk of their investments in the Phoenix securities, Shuler attempted, for the first time, to explain the Blue Contract Misrepresentations. To the shock and surprise of Zawatsky, who as a result of Trust Communities Inc.'s \$2 million dollar loan to Phoenix had been added as a member of the Phoenix Board of Directors, Shuler indicated that the Phoenix "contracts" were not for a firm number of products or dollars, but were essentially options given to purchasers to order, at a purchaser's discretion, products covered by a contract.

56. In the second half of May 2002, Levy and Phoenix forwarded to Rolinski in Maryland by US mail the May 2002 Contracts Statement.

57. In or around June of 2002, Levy telephoned Rolinski in Maryland and told her that Phoenix had been awarded a \$10 million U.S. Department of Defense contract for the delivery of "sensors" (the "DOD Sensor Contract"). Rolinski queried Levy about the Contracts Statements. Levy made the Blue Contract Misrepresentations to Rolinski in that telephone conversation and urged Rolinski to invest further in Phoenix. Levy did not correct the Border Contract Misrepresentation. On the basis of the Blue Contract Misrepresentations, and continuing to rely on the Border Contract Misrepresentation, Rolinski, on June 24, 2002, purchased an additional 900 shares of Phoenix common stock at \$5.00 per share.

58. The Blue Contract Misrepresentations were material to Rolinski's decision to invest in Phoenix, and the truth would have assumed actual significance in Rolinski's decision to invest in Phoenix. Rolinski would not have invested for the second time in

Phoenix but for the Blue Contract Misrepresentations, and but for the Border Contract Misrepresentation and the failure to correct the Border Contract Misrepresentation.

59. On or around July 1, 2002, Levy telephoned Zawatsky in his office in Washington, D.C. and told Zawatsky that Levy had "great news." Levy advised Zawatsky that Phoenix had secured the DOD Sensor Contract, and Levy urged Zawatsky to invest further in Phoenix on behalf of I&B. Levy did not correct the Blue Contract Misrepresentations. Zawatsky asked Levy when revenue would be generated from the DOD Sensor Contract. Levy stated that sensors would begin to be shipped immediately. Levy also stated that the cash flow generated by the sensor sales pursuant to the \$10,000,000 contract would allow Phoenix to pay the investors a dividend of nearly all of the \$5.00 per share price by December of 2002. As is more fully set forth in paragraph 60 below, the Phoenix Board of Directors subsequently passed a resolution setting out the Phoenix policy on declaration of dividends.

As a result of Levy's statements, as set forth in the preceding paragraph, and the impact of that purported contract on Phoenix's immediate cash flow and its ability to pay dividends as promised, and as a result of the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, I&B, on July 8, 2002, purchased an additional 25,000 shares of Phoenix common stock at \$5.00 per share.

60. On July 16, 2002, Zawatsky and two advisers traveled to Florida to inspect the Phoenix facility and to meet with Shuler. During his inspection, Zawatsky specifically inquired of Shuler if Phoenix had the ability to meet the immediate, imminent, urgent and substantial production demands of the DOD Sensor Contract. Shuler made no attempt to advise Zawatsky that the DOD Sensor Contract production

requirements were not imminent, or did not require immediate and substantial production. Instead, Shuler showed Zawatsky the manufacturing facility and stated that hundreds of sensors could be completed and shipped per week by using three production shifts. Shuler represented to Zawatsky that Phoenix was capable of meeting immediately all of the production requirements of the DOD Sensor Contract. Neither Shuler nor anyone at Phoenix corrected the Blue Contract Misrepresentations, or indicated that the DOD Sensor Contract was not for immediate production and sales, or that it gave the Department of Defense the right to order only a few sensors and was not a binding obligation of the Department of Defense to take and pay for \$10,000,000 of sensors in the short term (the “DOD Sensor Omission”).

On July 21, 2002, Shuler and the Phoenix Board of Directors passed a resolution adopting a “liberal and aggressive dividend policy...,” designing a procedure to “aggressively pursue” by the end of 2002 a plan to go public, and providing specifically that: “...(c) ... upon the culmination of the current Fiscal Year, the Board herein agrees to declare and pay a dividend to all shareholders of record up to a maximum of five dollars (\$5.00) per share....”

61. As a result of the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and as a further result of the July telephone conversation with Levy, see para. 59 above, and the statements of Shuler to Zawatsky in Florida, see para. 60 above, I&B, on July 22, 2002 purchased an additional 100,000 shares at \$5.00 per share.

62. The Blue Contract Misrepresentations, the failure to correct the Blue Contract Misrepresentations, and the statements made by Shuler to Zawatsky in Florida were

material to I&B's decision to invest in Phoenix, and the truth would have assumed actual significance in I&B's decision to invest for the second and third time in Phoenix . I&B would not have invested a second and third time, increasing I&B's investment in Phoenix by a factor of 6 - from \$125,000 to \$750,000- if Levy and the Phoenix Defendants had not made the Blue Contract Misrepresentations, or if Levy or the Phoenix Defendants had corrected the Blue Contract Misrepresentations or had not made the DOD Sensor Omission.

63. On August 2, 2002, Phoenix prepared a written statement (the "August 2002 Contracts Statement") that purported to be an update of the September 2001 Contracts Statement and the May 2002 Contracts Statement . The August 2002 Contracts Statement was again color-coded in blue, yellow and green, and contained a legend identical to the legend in the September 2001 Contracts Statement and the May 2002 Contracts Statement. A true and accurate copy of the August 2002 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein, and the representations contained therein comprise in part the Blue Contract Misrepresentations. The August 2002 Contracts Statement identified 35 contracts. Of those contracts, 15 were highlighted in blue, 15 were highlighted in yellow, and 5 were highlighted in green. Blue highlighted contracts on the August 2002 Contracts Statement totaled \$1,981,075,523.

64. The August 2002 Contract Statements were delivered by Shuler through the means and instrumentalities of interstate commerce to I&B, Rolinski and Burman on or about August 12, 2002.

65. As is set forth in Paragraphs 52 through 55 above, the August 2002 Contracts Statement was false.

66. In or around January of 2003, Levy again telephoned Rolinski in Maryland and told her that Phoenix had procured a billion dollar contract with Egypt . Levy represented in that conversation with Rolinski that Shuler had gone to Egypt personally and procured the contract (the “Egypt Contract Misrepresentation”). In that telephone conversation, Rolinski and Levy discussed the Addendum E risk adjusted revenues. Levy told Rolinski that “investing in Phoenix carries a non-existent risk factor,” (the “Risk Factor Statement”) based on Addendum E. Levy did not correct the Border Contract Misrepresentation, or the Blue Contract Misrepresentations. Based on the Border Contract Misrepresentation, and the failure to correct the Border Contract Misrepresentation, and the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and the Egypt Contract Misrepresentation, and the Risk Factor Statement, Rolinski, on January 15, 2003, purchased 2000 shares of Phoenix common stock at \$10.00 per share, more than doubling her previous investment.

67. The Border Contract Misrepresentation, and the failure to correct the Border Contract Misrepresentation, and the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and the Egypt Contract Misrepresentation and the Risk Factor Statement were material to Rolinski’s decision to invest in Phoenix for the third time, and the truth would have assumed actual significance in Rolinski’s decision to invest in Phoenix for the third time, more than doubling her extant investment in Phoenix securities. Had Levy not made the Border Contract Misrepresentation, and failed to correct the Border Contract Misrepresentation, and had Levy and the Phoenix

Defendants not made the Blue Contract Misrepresentations, and failed to correct the Blue Contract Misrepresentations, and had Levy not made the Egypt Contract Misrepresentation and the Risk Factor Statement, Rolinski would not have invested in Phoenix for the third time.

68. These misrepresentations were false when made. The allegations of falsity are set out in Paragraphs 52 through 55 above.

69. In addition, as further evidence of the falsity of the Egypt Contract Misrepresentation, the allegations of falsity are based upon Shuler's statements in the March 4, 2003, investor update letter which reads in pertinent part, "In December 2002, I traveled to Egypt with the expressed purpose of signing the first delivery order for our approximate \$600 million National Intelligence Support System (NISS). *We have submitted all of the required information to the Ministry of Interior and are waiting as the project moves through their bureaucracy in order for it to receive all of the required approvals.*" Emphasis in original. Phoenix's own documents confirm that no contract was signed in January of 2003 with Egypt and in fact that the proposal was not for a billion dollar contract, but, at best, a \$600 million dollar proposal.

The Warriner Transaction

70. Plaintiff Warriner had multiple telephone conversations with Levy. Warriner was in his office in Washington DC for those telephone conversations.

71. In August 2002, in a telephone conversation with Levy while Warriner was in the District of Columbia, Levy made to Warriner the Egypt Contract Misrepresentation.

72. On August 27, 2002, on the basis of the statements made by Levy and the Egypt Contract Misrepresentation, Warriner purchased 5000 shares of Phoenix common stock at \$5.00 per share.

73. The Egypt Contract Misrepresentation was material to Warriner's decision to invest in Phoenix and the truth would have assumed actual significance in Warriner's decision to invest in Phoenix. Had Levy not made the Egypt Contract Misrepresentation, Warriner would not have invested in Phoenix.

The Burman Transactions

74. In the summer of 2001, Plaintiff Burman, at age 83, traveled to Florida to inspect the Phoenix facilities, and to meet with Shuler and Levy. Levy and Shuler advised Burman that Phoenix had a "secret facility" and that most of Phoenix's products and contracts were "classified" and could not be seen without top security clearances. During that visit, Levy represented to Burman that Phoenix had negotiated the DOD Sensor Contract.

75. In September 2001, prior to the purchase by Burman of Phoenix securities, Levy and the Phoenix Defendants delivered to Burman the September 2001 Contracts Statements, see para. 39 above.

76. Burman purchased 61,400 shares of common stock in Phoenix at \$5.00 for \$307,000 in 12 successive transfers, as follows: September 25, 2001, in the amount of \$20,000; on September 25, 2001, in the amount of \$2000; on November 3, 2001, in the amount of \$25,000; on December 19, 2001, in the amount of \$50,000; on March 1, 2002, in the amount of \$30,000; on May 20, 2002, in the amount of \$20,000; on August 2, 2002, in the amount of \$50,000; on August 28, 2002, in the amount of \$50,000; on

August 30, 2002, in the amount of 10,000; on September 1, 2002, in the amount of \$25,000; on September 1, 2002, in the amount of \$12,500; and, on September 1, 2002, in the amount of \$12,500.

77. In August of 2002, Burman was provided with the August 2002 Contracts Statement.

78. Prior to September 2002, Levy made to Burman in his office in Washington, D.C., by telephone, the Egypt Contract Misrepresentation. Levy never corrected the statements made in the September 2001 or August 2002 Contracts Statements, and never corrected the Egypt Contract Misrepresentation.

79. The Egypt Contract Misrepresentation, the September 2001 and August 2002 Contracts Statements were material as of the date that they were made to Burman's decisions to invest in Phoenix, and the truth would have assumed actual significance in Burman's decision to invest in Phoenix.

80. After making his investment in Phoenix on September 1, 2002, Burman asked Levy when Phoenix would receive payment under the DOD Sensor Contract. Levy finally informed Burman that the DOD Sensor Contract was not a binding obligation, but merely gave DOD the right to acquire at its discretion, up to \$10 Million in sensors from Phoenix.

81. The Contract Misrepresentations were false when made, and were known by Levy and by the Phoenix Defendants to have been false when made. The Phoenix Defendants acted with scienter in that they knew that the statements made by Levy and Shuler were materially false and misleading. They also knew that the documents issued and/or disseminated in the name of Phoenix were materially false and misleading.

Phoenix and Shuler also knew that such statements or documents would be issued or disseminated to the Plaintiffs and were in fact issued and disseminated to the Plaintiffs. They also knew and intended that the Plaintiffs would rely on such misstatements and documents, and they knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements and documents. The Contract Misrepresentations are: the Border Contract Misrepresentation; the Blue Contract Misrepresentations; the Egypt Contract Misrepresentation. The Blue Contract Misrepresentations include the oral statements as set forth above, Addendum E, and the Contracts Statements.

- 82. Shuler had a motive to make the Contract Misrepresentations.
- 83. Shuler had the opportunity to make the Contract Misrepresentations.
- 84. Phoenix had a motive to make the Contract misrepresentations.
- 85. Phoenix had the opportunity to make the Contract Misrepresentations.
- 86. In reasonable reliance on the misrepresentations and omissions of the Phoenix Defendants, Plaintiffs transferred to Phoenix a total of \$1,116,500 in exchange for a total of 223,300 shares of Phoenix securities.

The IRS Misrepresentations

- 87. In connection with the sale of Phoenix's securities, the Plaintiffs were provided with the Company's audited financial statements prepared by R&C.
- 88. The financial statements dated March 31, 2002-2001, contain notes to the financial statements. Specifically, Note 10, titled "Commitments and Contingencies" contains an averment regarding payroll taxes. Note 10 reads in pertinent part, "Included in accounts payable and accrued expenses at year end are accrued payroll taxes. The

payroll taxes were past due and the Company may be subject to penalties and Interest. No penalties or interest has been imposed. In August 2002 past due payroll taxes were paid (see Note 13)". Note 13, titled "Subsequent Events", makes further representations regarding the unpaid employment taxes. Note 13 reads in pertinent part, "The Company's payroll taxes were past due at year end (see Note 10). In August 2002, the Company paid all current and overdue payroll taxes."

89. In May 2002, after reviewing the March 31, 2001-2000 audited financial statements, which indicated in Note 9 unpaid employment taxes, Zawatsky questioned Levy about such unpaid employment taxes. Zawatsky was told by Levy that the unpaid employment taxes had in fact been paid in 2002, after March 31. That statement by Levy was false.

90. During his visit to Phoenix on July 16, 2002, Zawatsky asked Shuler directly about the unpaid employment taxes. Shuler told Zawatsky that the unpaid employment taxes had been paid and that the March 31, 2002-2001 audited financial statements would reflect that payment (along with the financial statements, the "IRS Misrepresentations"). As set forth in para. 88, the March 31, 2002-2001 audited financial statements prepared by R&C as of June 12, 2002, and September 26, 2002, did represent in Notes 10 and 13 that the unpaid employment taxes had been paid in August, 2002. Shuler's statement that the unpaid employment taxes had been paid was false.

91. As evidence of the falsity of the IRS Misrepresentations, on or around, April 13, 2004, a letter was sent to Robert Pugh, CPA, the CFO of Trust Communities, Inc., from the IRS stating that Phoenix was liable for unpaid employment taxes (Forms 940 and 941) from the 1998-2003 tax years and that the IRS had placed a tax lien against

Phoenix's real property. The letter stated, "The amount needed to fully pay all liabilities and release the lien is \$233,677.95." A true and correct copy of the April 13, 2004 letter is attached hereto as Exhibit 3 and it is adopted and incorporated herein as is specifically set forth herein.

92. The Phoenix Defendants and R&C issued materially false and misleading financial statements and omitted to disclose material information regarding the status of Phoenix's unpaid employment taxes (Forms 940 and 941) from the 1998-2003 tax years.

93. The Phoenix Defendants knew and should have known that they owed to the IRS at the time that they made the IRS Misrepresentations unpaid employment taxes and should have disclosed this fact to the Plaintiffs prior to their investments.

94. When Phoenix's financial statements were audited by R&C for the referenced time periods, R&C should have disclosed the unpaid taxes in its audit reports. R&C audit reports for 1999-2003 were provided to the Plaintiffs by the Phoenix Defendants and R&C, but the 2002-2001 and 2003-2002 audited financial statements failed to disclose the unpaid employment taxes. Indeed, the 2002-2001 audited statements reported that the taxes had been paid. According to R&C, Phoenix was responsible for making its tax payroll payments and "many of them had been made late" for the period of 1999 to 2004". See Declaration of Carl N. Howden, December 24, 2004, appended to Rachlin Reply Memorandum In Support of Suggestion of Responses of Motion to Dismiss, filed December 23, 2004.

According to R&C, Phoenix paid over \$16,000 in payroll tax liabilities no earlier than November 15, 2004, but arising out of claimed deficiencies from 1999-2004.

95. The Phoenix Defendants and R&C failed to disclose to Plaintiffs the unpaid taxes. Zawatsky called R&C immediately after Zawatsky learned of the IRS tax lien and the unpaid employment taxes. Zawatsky was told that R&C would have Carl Howden ("Howden") "get right on" the unpaid tax issue. Zawatsky later spoke with Howden who acknowledged that he had not resolved the issue. Plaintiffs, prior to the initiation of this litigation, were never supplied with any additional information concerning the unpaid employment taxes, and the Phoenix Defendants failed to correct the IRS Misrepresentations prior to the initiation of this litigation.

96. The failure to disclose the unpaid taxes was material to each Plaintiff's decision to invest in Phoenix, and the truth would have accrued actual significance in their decisions to invest in Phoenix. Had the Phoenix Defendants or R&C disclosed the unpaid employment taxes, no Plaintiff would have invested in Phoenix.

Count 1

(Violation of Section 10(b) Of the Exchange Act And Rule 10b-5 Promulgated Thereunder By Defendants Phoenix and Shuler)

97. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 96 of the Second Amended Complaint as if fully set forth herein.

98. The Phoenix Defendants carried out a plan, scheme and course of conduct which was intended to and did deceive the Plaintiffs as alleged herein and cause the Plaintiffs to purchase Phoenix securities. In furtherance of this unlawful scheme, plan and course of conduct, the Phoenix Defendants took the actions set forth herein.

99. The Phoenix Defendants employed devices, schemes, and artifices to defraud, directly and indirectly, caused false statements to be made to the Plaintiffs as specified

herein and failed to state material facts to the Plaintiffs as set forth herein, and engaged in acts, practices, and a course of business which operated as a fraud and deceit upon the Plaintiffs in violation of Section 10(b) of the Exchange Act and Rule 10b-5.

100. The Phoenix Defendants, directly and indirectly, by the use, means or instrumentalities of interstate commerce, including use of the telephones, mails, wires and the Internet, disseminated the materially false statements and omissions referenced herein. The initial definitions of such statements and omissions are set out in paragraphs 16, 17, 40, 49, 66 and 81.

101. The Phoenix Defendants knew and should have known that the Contract Misrepresentations and the IRS Misrepresentations (collectively, “the Misrepresentations”) specified above were untrue when made and that the truth and the omissions would have been material to the Plaintiffs’ decision to participate in the offering of Phoenix securities. The Phoenix Defendants made the Misrepresentations, and omitted the omissions, knowingly and willfully, and with such extreme recklessness that the misconduct rose to the level of fraud.

Defendant Shuler had an improper motive to mislead Plaintiffs, including the desire to minimize his personal liability, and to minimize the risk to his personal investment in Phoenix, and to maximize his personal profit from Phoenix, at the risk and at the expense of Plaintiffs. Defendant Shuler had multiple opportunities to mislead Plaintiffs, including his exercise of complete control over Phoenix, and its agents.

Defendant Phoenix had an improper motive to mislead Plaintiffs, including the improper desire of Phoenix to advance and to protect the personal interests of Shuler, and to induce Plaintiffs to invest monies in Phoenix without meaningful disclosure of

Phoenix's financial position, and then-existing contractual commitments. Defendant Phoenix had multiple opportunities to mislead Plaintiffs by its direct and complete control, through its officers and agents, of information material to the decisions of the Plaintiffs to purchase Phoenix securities.

The Misrepresentations were made by the Phoenix Defendants, using fraudulent means, and material facts were concealed from the Plaintiffs with the specific intent to cause the Plaintiffs to transfer funds to Phoenix in exchange for Phoenix securities.

102. At the time of the described Misrepresentations, Plaintiffs were ignorant of their falsity and believed them to be true and had no knowledge of the existence of the material factual omissions.

103. Plaintiffs reasonably relied upon the Misrepresentations of the Phoenix Defendants and, as a consequence, transferred \$1,116,500, in the specific sums and on the specific dates set out herein, to Phoenix in exchange for Phoenix securities.

104. The conduct of the Phoenix Defendants, described above, constitutes a violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.

105. As a direct and proximate result of the wrongful conduct of the Phoenix Defendants, Plaintiffs suffered damages in connection with their purchases, as set forth herein, of Phoenix securities, in an amount equal to the purchase price of the securities.

Count Two
**(Common Law Fraud, Deceit and Misrepresentation
 By Defendants Phoenix and Shuler)**

106. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 105 of the Second Amended Complaint as if fully set forth herein.

107. To induce the Investors to transfer \$1,116,500 to Phoenix in exchange for Phoenix Securities, the Phoenix Defendants made to Plaintiffs, at the times and in the places set forth herein, the Contract Misrepresentations and the IRS Misrepresentations, and continuously thereafter failed and refused to correct the Misrepresentations. The initial definitions of such Misrepresentations are set out in paragraphs 16, 17, 40, 49, 66 and 81.

108. When the Phoenix Defendants made these Misrepresentations to Plaintiffs, the Phoenix Defendants knew they were false and misleading, and the Misrepresentations were made with the intent to deceive Plaintiffs and induce Plaintiffs to purchase Phoenix securities, and the Misrepresentations were made with such extreme recklessness and disregard for the truth as to rise to the level of fraud.. The Phoenix Defendants also knew that by failing to state facts material to Plaintiffs' decisions to participate in the offering, and by failing to correct the Misrepresentations, the Phoenix Defendants were misleading Plaintiffs, and the Phoenix Defendants did so with the intent to deceive Plaintiffs and induce Plaintiffs to purchase Phoenix securities.

109. Plaintiffs reasonably relied on the Misrepresentations and failures to state material facts, and failures to correct the Misrepresentations, and in reliance thereon, Plaintiffs transferred \$1,116,500 to Phoenix for the purchase of securities in the sums and on the dates set forth herein.

110. But for the Misrepresentations and failures to state material facts, and failures to correct the Misrepresentations, by the Phoenix Defendants, Plaintiffs would not have purchased any Phoenix securities, and Plaintiffs relied to their detriment on the Misrepresentations and failures to state material facts, and failures to correct the

Misrepresentations. The Phoenix securities purchased by Plaintiffs are worth, if anything, substantially less than the price paid by Plaintiffs to purchase the securities.

111. The acts and omissions of the Phoenix Defendants, as set forth above, directly and proximately caused damages to Plaintiffs, and as a result, the Plaintiffs lost \$1,116,500, collectively, plus interest thereon, since the dates of Plaintiffs' investments, in the amounts and on the dates set forth herein.

112. The willful and intentional fraud of Defendants Phoenix and Shuler is accompanied by such a high degree of scienter as to render the Phoenix Defendants liable for punitive damages in an amount to be proven at trial, but in any event not less than \$100,000.00 for each plaintiff.

Count Three

(Negligent Misrepresentation By Defendants Phoenix and Shuler)

113. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 112 of the Second Amended Complaint as if fully set forth herein.

114. To induce the Investors to transfer \$1,116,500 to Phoenix in exchange for Phoenix securities, the Phoenix Defendants made to Plaintiffs at the times and in the places set forth herein, the Contract Misrepresentations and the IRS Misrepresentations, and failed to state material facts to Plaintiffs, and continuously thereafter failed and refused to correct the Misrepresentations, and made the Public Sale Statements, the Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission (the "Status Statements"). The initial definitions of such Misrepresentations and Statements are set out in paragraphs 16, 17, 40, 49, 50, 60, 66, 81 and 114.

115. No dividends have been declared, paid or issued by Phoenix to Plaintiffs.

116. No public sale has been undertaken, nor the planning for any public sale concluded.

117. The risks associated with the purchase of the securities were and are well in excess of zero.

118. The DOD Sensor Contract was not, in 2002, for immediate production and sale, and did not, according to the subsequent and belated statements of the Phoenix Defendants, bind DOD to purchase sensors in any specific volume or dollar amount.

119. When the Phoenix Defendants made these Misrepresentations and failed to state material facts to Plaintiffs, and failed to correct the Misrepresentations, and made the Status Statements, they knew or should have known they were false and misleading and that Plaintiffs would rely thereon in order to decide whether to purchase Phoenix securities.

120. Plaintiffs did in fact rely on the Misrepresentations and the failures to state material facts, and the failure to correct the Misrepresentations, and the Status Statements as set forth herein, and such reliance was objectively reasonable. Reliance on the Misrepresentations and the failures to state material facts and the failure to correct the Misrepresentations, and the Status Statements was material to the investment decisions made by the Plaintiffs.

121. The acts and omissions of the Phoenix Defendants, as set forth herein, directly and proximately caused damages to Plaintiffs, and as a result, the Plaintiffs lost \$1,116,500, collectively, plus interest thereon, since the dates of Plaintiffs' investments, in the amounts and on the dates set forth herein.

Count Four
(Breach of Fiduciary Duties By Defendants Phoenix and Shuler)

122. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 117 of the Second Amended Complaint as if fully set forth herein.

123. The Phoenix Defendants owed to Plaintiff Burman fiduciary duties of loyalty, diligence and fairness commencing September 25, 2001.

124. The Phoenix Defendants owed to Plaintiff Rolinski fiduciary duties of loyalty, diligence and fairness commencing February 20, 2002.

125. The Phoenix Defendants owed to Plaintiff I&B fiduciary duties of loyalty, diligence, disclosure and fairness commencing May 28, 2002.

126. The Phoenix Defendants owed to Plaintiff Warriner fiduciary duties of loyalty, diligence, good faith and fairness commencing August 27, 2002.

127. The Phoenix Defendants breached their fiduciary duties by making the Contract Misrepresentations.

128. The Phoenix Defendants breached their fiduciary duties by failing to correct the Contract Misrepresentations.

129. The Phoenix Defendants breached their fiduciary duties by making the IRS Misrepresentations.

130. The Phoenix Defendants breached their fiduciary duties by failing to correct the IRS Misrepresentations.

131. The Phoenix Defendants breached their fiduciary duties by making the the Public Sale Statements, the Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission.

132. The Phoenix Defendants breached their fiduciary duties by failing to correct the Public Sale Statements, the Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission.

133. The initial definitions of such Misrepresentations and Statements are set out in paragraphs 16, 17, 40, 49, 50, 60, 66, 81 and 114.

134. As a direct, proximate and foreseeable consequence of these breaches of fiduciary duty, Plaintiffs Burman, Rolinski and I&B were wrongly induced to purchase additional shares of Phoenix stock which are now worthless of nearly worthless.

Count Five
(Violation of State Blue Sky Laws By Defendants Phoenix and Shuler)

135. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 133 of the Second Amended Complaint as if fully set forth herein, and restate with particularity the averments of Count One herein as if they are repeated verbatim in this Count..

136. The Misrepresentations made by the Phoenix Defendants, and the failure to state material facts, and failure to correct the Misrepresentations, were in violation of the blue sky state security statutes of the District of Columbia, D.C. Code § 3-3602 (2001), 31-5605.02 (2001, Replacement Vol. 2005) and the State of Maryland. Section 11-301 of the Maryland Securities Act. The initial definitions of such Misrepresentations are set out in paragraphs 16, 17, 40, 49, 66 and 81.

137. Plaintiffs sustained injury and damage as a consequence of the violations by the Phoenix Defendants of the blue sky state securities statutes of the District of Columbia and the State of Maryland, including the loss of monies paid to Phoenix, in the amounts and on the dates set forth herein, for the purchase of Phoenix securities.

Count Six
(Appointment of a Receiver for Phoenix)

. 138. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 136 of the Second Amended Complaint as if fully set forth herein.

139. Phoenix has failed and refused, despite repeated demands, to convene a shareholders' meeting. A shareholders' meeting is a requirement of state law, including Florida law. Following repeated demands a shareholders' meeting was scheduled for September 28, 2005. Phoenix cancelled the shareholders' meeting on September 15, 2005.

140. As of October 3, 2005, Phoenix has failed to prepare or distribute an audited financial statement for the fiscal year ending March 31, 2005.

141. Plaintiffs made repeated requests for a final audited financial statement for the fiscal year ending March 31, 2004 ("FY 2004"). Those requests were ignored until, on May 31, 2005, a copy of an audited financial statement for FY 2004 (the "FY 2004 Statement") was delivered to counsel of record for plaintiffs. A true and accurate copy of the FY 2004 Statement is appended hereto as Exhibit 4, and is adopted and incorporated herein.

142. Though purporting to reflect a period ending March 31, 2004, the FY 2004 Statement included a January 26, 2005 event, as well as several other events – related to payroll taxes - which took place after March 31, 2004.

143. Plaintiffs have received from Phoenix no financial information subsequent to receipt of the FY 2004 Statement.

144. The FY 2004 Statement showed:

- a. Cash and accounts receivable of \$313,079;
- b. Accounts payable and accrued liabilities of \$671,544;
- c. Current assets which were incorrectly inflated by out-of-date or non-current inventory;
- d. Receipt by Shuler from Phoenix, during the reported year, of \$352,000. That sum represented a salary increase of 33%, or \$48,000.

During the same period, accounts payable and accrued liabilities increased by \$571,986, from \$159,588 to \$671,544.

- e. Monthly selling, general and administrative expenses averaging \$113,660, or over one-third of all available cash and receivables.

145. Phoenix out of date on non-current inventory is valueless – or virtually valueless - because Phoenix builds to contract, and has not regularly sold out of “inventory”.

146. The debt described in the Second Amended Complaint, at para. 4, was replaced in or about January 2005 by new debt, and included an additional debt of \$400,000. Taking into account the origination fee, the new debt has an effective interest

rate of 15%. While the previous debt was secured by real estate, the new debt is secured by all Phoenix assets, and it is due in full February 1, 2006.

147. Phoenix is insolvent.

148. Phoenix is at great risk of further financial loss.

149. It is in the interest of Plaintiffs, and in the interest of all non-insider investors in Phoenix, and in the general public interest, that the court appoint a Receiver for Phoenix, who will:

- a) examine and correct the public statements of Phoenix;
- b) examine and secure, to the extent possible, the contracts, and income from the contracts identified by Phoenix on Addendum E and the Contracts statements;
- c) examine, terminate or suspend, and report to the court on the payments, if any, by Phoenix to Shuler, or to R&C, or to Levy;
- d) prepare, complete and disseminate to Plaintiffs and to the court a comprehensive financial statement for Fiscal Years 2001 through 2005;
- e) pay all outstanding taxes; and
- f) take such other actions as are necessary and appropriate to the protection of the non-insider shareholders of Phoenix.

Count Seven
(Injunctive Relief Against the Phoenix Defendants)

150. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 138 of the Second Amended Complaint as if fully set forth herein.

151. The balance of equities weighs in favor of full disclosure of the financial condition of Phoenix.

152. The public interest weighs in favor of full disclosure of the financial condition of Phoenix.

153. Plaintiffs are entitled as a matter of equity to a preliminary and a permanent injunction, decree and order directing the Phoenix Defendants to:

- a) correct the public statements of Phoenix;
- b) terminate or suspend, and report to the court on the payments, if any, by Phoenix to Shuler, or to R&C, or to Levy; and
- c) prepare, complete and disseminate to Plaintiffs and to the court a comprehensive audited financial statement for Fiscal Years 2001 through 2005.

Count Eight

(Negligence Against Defendant R&C)

154. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 142 of the Second Amended Complaint as if fully set forth herein.

155. R&C owed a duty to Plaintiffs to act with the requisite degree of skill and care that reasonably competent public accountants follow when auditing the financial statements of a company for presentation to potential investors.

156. When R&C audited the financial statements of Phoenix, they reasonably should have discovered that Phoenix had unpaid employment taxes (Forms 940 and 941) for the 1998 through 2003 tax years.

157. Because R&C either did not discover the unpaid employment taxes of Phoenix and/or did not adequately report such information in the audited financial statements, R&C breached its duty to Plaintiffs by falling below the standard of care applicable to accountants in the same or similar situation.

158. By not following that standard of skill and care, R&C's conduct was the direct and proximate cause of injury to the Plaintiffs. Plaintiffs would not have invested in Phoenix securities had R&C's audit reports disclosed the existence of unpaid employment taxes.

159. As a direct and proximate result of the negligence of R&C, Plaintiffs suffered damages in the amount of \$1,116,500, collectively, plus interest in the amount of 10% per annum, since the respective dates of Plaintiffs' investments.

WHEREFORE, Plaintiffs pray for relief and judgment as follows:

- a) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Burman against all Defendants, jointly and severally, in the amount of \$307,000.00, or such other amount as may be proven at trial;
- b) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Warriner against all Defendants, jointly and severally, in the amount of \$25,000.00, or such other amount as may be proven at trial;
- c) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff I&B against all Defendants, jointly and severally, in the amount of \$750,000.00, or such other amount as may be proven at trial;

- d) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Rolinski against all Defendants, jointly and severally, in the amount of \$34,400.00, or such other amount as may be proven at trial;
- e) As to Counts Two and Four, an award of punitive damages, in an amount to be proven at trial, in favor of all Plaintiffs and against Defendant Phoenix.
- f) As to Counts Two and Four, an award of punitive damages, in an amount to be proven at trial, in favor of all Plaintiffs and against Defendant Shuler.
- g) As to Count One, an award of statutory damages;
- h) As to Count Five, an award of statutory damages;
- i) As to Counts One, Two, Four and Five, an award in favor of Plaintiffs and against the Phoenix Defendants, jointly and severally, of the reasonable attorneys fees incurred by Plaintiffs in the prosecution of this action;
- j) As to Count Six, the appointment of a receiver to take the actions set forth in Count Six;
- k) As to Count Seven, the entry of an injunction, decree, order or judgment directing the Phoenix Defendants to take the actions set forth in Count Seven;
- l) As to Count Eight, compensatory damages in favor of plaintiffs, in the amounts set forth in (a), (b), (c), and (d), above, against Defendant R&C;
- m) An award to Plaintiffs of costs;
- n) An award to Plaintiffs of prejudgment interest and post judgment interest; and
- o) Such other and further relief as the Court may deem just and proper.

Jury Demand

Plaintiffs demand a trial by jury of all issues so triable in this action.

Respectfully Submitted,

Rolinski, Terenzio & Suarez, LLP



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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was sent by electronic mail this 3rd day of October 2005 to the following: Luis S. Konski, Esq. Becker & Poliakoff, P.A., 121 Alhambra Plaza, 10th Floor, Coral Gables, Florida 33134; Kenneth A. Martin Esq. Martin & Associates, P.L.L.C., 1827 Jefferson Place, NW, Washington, DC 20036, and Thomas S. SchaufelbergerEsq. and Paul A. Fitzsimmons, Esq., Wright, Robinson, Osthimer & Tatum 5335 Wisconsin Avenue, Washington, DC 20015.



Philip M. Musolino

EXHIBIT 1

ADDENDUM E

Financial Projections

Phoenix Worldwide Industries, Inc.



RISK ADJUSTED PROJECTED REVENUE

REVENUE ITEM:	AMOUNT	BASIS & ASSUMPTION	%	YR 1	%	YR 2	%	YR 3
1 ONGOING BUSINESS	2,000,000	RENEWAL, REPLACEMENT, UPGRADES OF EXISTING PRODUCT BASE ON A ANNUAL BASIS WITH SOME ADDITIONAL MARKETING AND COMMUNICATION	100%	2,000,000	100%	2,000,000	100%	2,000,000
2 DIRECT LAW ENFORCEMENT	1,000,000	WITH CAPITAL THE COMPANY HAS AN UNSERVICED DEMAND THAT IS TIME DEPENDENT. THIS IS MUNICIPAL AND REGIONAL POLICE AGENCIES. WE BELIEVE THAT IT IS REASONABLE THAT A SALESMAN THAT IS FOCUSED ON THIS SEGMENT CAN GENERATE A MILLION DOLLARS IN ORDERS A YR. WE WILL ADD ONE SALESMAN A YR.	100%	1,000,000	100%	2,000,000	100%	3,000,000
3 GOVERNMENT AGENCIES	3,000,000	COMPANY HAS RECEIVED A NUMBER OF REQUESTS FOR PROPOSALS THAT ARE NOT BEING ATTENDED. IN ADDITION WE ARE CONSTANTLY FINDING AGENCIES THAT ARE NOT AWARE OF COMPANY CAPABILITIES. AN ASSIGNED SALES FORCE SHOULD BE ABLE TO GENERATE ANNUAL SALES OF 3 MILLION DOLLARS ANNUALLY. WE WILL START WITH 2 ACCOUNT EXEC. AND ADD ONE EACH YEAR	100%	6,000,000	100%	9,000,000	100%	12,000,000

PENDING PROPOSALS:

4 D.A.S. COLOMBIA (NIS)	472,572,610	PROJECT HAS BEEN APPROVED BY HEAD OF DAS, THE MINISTER, THE PRESIDENT, AND THE AMBASSADOR. PROJECT IS AWAITING FUNDING. WITH ALL THE SOURCES OF FUNDING FOR ANTI DRUG WE HAVE A HIGH CONFIDENCE FACTOR. WE BELIEVE THE ORDER WILL COME IN OVER TWO YEARS.	80%	189,029,044	90%	212,657,675	
5 WHITE HOUSE COMMUNICATIONS AGENCY (WHCA)	30,000,000	PROJECT HAS BEEN VERBALLY APPROVED THE AGENCY IS SMALL AND REQUIRES SUPPORT IN PACKAGING PROJECT FOR BUDGET INCORPORATION. THE COMPANY IS SLOWLY SUPPLYING ASSISTANCE. ADDITIONAL INFRASTRUCTURE WOULD ACCELERATE PROJECT INCORPORATION. DELIVERY OVER TWO YEARS	90%	13,500,000	95%	14,250,000	
6 EGYPTIAN PRESIDENTIAL GUARDS PRESIDENTIAL AND DIGNITARY PROTECTION	19,540,000	PROJECT HAS BEEN APPROVED AT HIGHEST LEVEL. CURRENTLY GOING THRU ADMINISTRATIVE PROCESS FOR ORDER. ESTIMATE 120 DAYS. DELIVERY IN NINE (9) MOS. PROJECT NEEDS FOLLOW UP AND ATTENTION	90%	17,588,000			
7 PROJECTS THAT REQUIRE COMMUNICATIONS AND FUNDING ASSISTANCE	827,002,068	(SEE ATTACHED SCHEDULE)	10%	82,700,207	25%	206,750,517	45%
8 PROJECTS THAT REQUIRE COMMUNICATIONS AND FUNDING ASSISTANCE IN ADDITION TO ADDITIONAL MARKETING AND ENGINEERING.	1,529,973,181	(SEE ATTACHED SCHEDULE)	5%	76,498,659	10%	152,997,318	20%
TOTAL	2,885,087,858			599,655,509		388,313,910	695,145,567

PROJECTS REQUIRING FUNDING

PROJECT	AMOUNT	PROBABILITY	ADJUSTED
CISEN MEXICO (NISS)	472,572,610	PROJECT WAS REQUESTED BY NEW PRESIDENT. PROJECT REQUIRES SUPPORT AND ASSISTANCE IN THE ADMINISTRATIVE PROCESS OF THE BUDGET WITH ITS ATTENDANT LOBBYING. IN ADDITION FOREIGN FUNDS ARE AVAILABLE FOR ANTI DRUG EFFORTS.	80% 378,058,068
SIDE ARGENTINA	472,572,610	PROJECT HAS BEEN VERBALLY APPROVED AT ALL LEVELS. IT IS CURRENTLY AWAITING FUNDING.	35% 165,400,414
CARBINEROS CHILE	472,572,610	PROJECT HAS BEEN VERBALLY APPROVED AT ALL LEVELS. IT IS CURRENTLY AWAITING FUNDING. COUNTRY HAS EXISTING FUNDS AVAILABLE IN BUDGET. THE PROJECT REQUIRES ATTENTION AND LOBBYING. SOME PORTION WILL DEFINITELY BE FUNDED	60% 283,543,566
TOTALS	1,417,717,830		827,002,068

PROJECTS REQUIRING MARKETING

PROJECT	AMOUNT	PROBABILITY	ADJUSTED
INTEL URUGUAY	236,286.305	60%	141,771.783
BAHRAIN INTERNAL SECURITY	110,179.842	40%	44,071.937
MOROCCO INTERNAL SECURITY	362,554.862	50%	181,277.431
BRAZIL INTERNAL SECURITY	472,572.610	45%	212,657.675
EGYPT INTERNAL SECURITY	472,572.610	50%	236,286.305

UAE INTERNAL SECURITY	569,952,787	PROJECT APPROVED AT DEPAKI MEDI LEVEL. DEPT. NEEDS SUPPORT FOR LOBBYING AND FINANCE DEMONSTRATION PROJECT	40%	249,949,554
KUWAIT INTERNAL SECURITY	499,889,108	PROJECT APPROVED AT DEPARTMENT LEVEL. DEPT. NEEDS SUPPORT FOR LOBBYING AND FINANCE DEMONSTRATION PROJECT	50%	249,949,554
LEBANON BORDER TEST BED & PRESIDENTIAL SECURITY	45,389,700	PROJECT REQUIRES ADDITIONAL REFINEMENT AND DEMONSTRATION. DEPARTMENT HEAD SUPPORTS PROJECT BUT REQUIRES ASSISTANCE IN SELLING TO UPPER GOVERNMENT.	55%	24,984,335
JORDAN PRESIDENTIAL SECURITY	39,970,914	VERBAL APPROVAL AT HIGHEST LEVEL BUT PROJECT REQUIRES DEMONSTRATION MARKETING, AND FINANCE ASSISTANCE	55%	21,984,003
QATAR INTERNAL SECURITY	236,286,305	STRONG DEPARTMENT SUPPORT. PROJ. REQUIRES MARKETING ASSISTANCE TO GARNER APPROVAL AT UPPER ADMINISTRATIVE LEVELS. DEMONSTRATION PROJECT	40%	94,514,522
SRI-LANKA INTERNAL SECURITY	236,286,305	STRONG SUPPORT AND NEED DUE TO TAMIL UPRISING. PROJECT REQUIRES FUNDING SUPPORT	40%	94,514,522
TOTALS	3,281,951,348			1,529,973,181

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EXHIBIT 2*

*** Plaintiffs adopt and incorporate herein by reference as if specifically appended hereto the full-color versions of Exhibit 2 which were appended as Exhibit 2 to the initial Complaint.**

9/03/01

PHOENIX WORLDWIDE INDUSTRIES

CONTRACTS IN PROGRESS

Contracts as of 09/03/2001

Verify to Invoices
& A/R

Scheduled

Completed

E/P

Scheduled

Contract Start Date	Estimated Contract Completion Date	Contract Number/ Description	Total Contract Price	Contract Billings to Date	Contract Costs Incurred to Date	Percent Completed	% Gross Profit to Date	Estimated Cost to Complete
10/01/2001	01/22/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	100,000.00	100,000.00	10%	0.00	800,000.00
10/14/2001	01/18/2002	DSEN - Venezuela	1,200,000.00	120,000.00	120,000.00	10%	0.00	980,000.00
10/15/2001	11/15/2001	Police Fiscal	719,542.14	719,542.14	719,542.14	100%	0.00	319,875.00
11/16/2001	02/16/2002	Ejercito de Colombia	975,000.00	975,000.00	975,000.00	100%	0.00	438,750.00
11/26/2001	01/25/2002	DANEK/Mexico	230,186.37	230,186.37	230,186.37	100%	0.00	99,196.27
05/01/2001	10/01/2002	TATTOO ID	3,701,000.00	3,701,000.00	3,701,000.00	100%	0.00	21,700.00
05/30/2001	01/15/2002	F0062001F0215-A1 Macdill Special Ops Command	33,580.00	0	0	0%	0.00	12,178.00
10/17/2001	02/17/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	100,000.00	100,000.00	10%	0.00	800,000.00
10/20/2001	11/20/2001	U.S. Dept. of Defense - Contracting Services - Venezuela	1,000,000.00	100,000.00	100,000.00	10%	0.00	800,000.00
01/12/01	03/12/01	U.S. Dept. of Defense - Contracting Services - Venezuela	39,120.00	0	39,120.00	100%	0.00	0.00
10/04/2001	02/24/2002	DISIE-Venezuela	750,000.00	0	0.00	0%	0.00	385,000.00
09/30/2001	12/16/2001	U.S. Customs - C-	525,000.00	0	0.00	0%	0.00	295,000.00
12/14/2001	03/31/2002	USA-PRRA Security Shelters	2,500,000.00	0	0	0%	0.00	1,120,000.00
12/03/2001	03/03/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/04/2001	05/04/2002	Saudi Air Force Weapons of Mass Destruction Detection Platforms.	45,000,000.00	0	0	0%	0.00	22,865,000.00
12/09/2001	06/20/2002	Egyptian Presidential Guard -C- Weapons of Mass Destruction and COMIAAN Platforms	16,998,186.80	0	0	0%	0.00	6,850,000.00
12/22/2001	03/22/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/23/2001	04/23/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/24/2001	05/24/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/25/2001	06/25/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/26/2001	07/26/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/27/2001	08/27/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/28/2001	09/28/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/29/2001	10/29/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/30/2001	11/30/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00
12/31/2001	12/31/2002	U.S. Dept. of Defense - Contracting Services - Colombia	1,000,000.00	0	0	0%	0.00	800,000.00

Note:

Bills = Billed Contracts

Open Contracts Pending

Note 1 - Awaiting funding from U. S. Congress - Plan Colombia

Note 2 - Awaiting Presidential Approval

Note 3 - Awaiting Final Approval

Note 4 - Awaiting Funding

Note 5 - Awaiting Final Approval

Note 6 - Awaiting Final Approval

Yellow = Contracts in Process of being Signed

6/16/2001

Note 1 - Awaiting funding from U. S. Congress - Plan Colombia

Note 2 - Awaiting Presidential Approval

Note 3 - Awaiting Final Approval

Note 4 - Awaiting Final Approval

Note 5 - Awaiting Final Approval

Note 6 - Awaiting Final Approval

PHOENIX-Defense, N.J.

EXHIBIT

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Yellow = Contracts In Process or being Signed

CHINESE CULTURE

Note 1 - Waiting funding from
U.S. Congress - Plan Colombia

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Note 2 - Awaiting Presidential Approval

Note 6 & 7 - This is a 5 year contract and the Total Contract Price is given as estates per annum.

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PHOENIX WORLDWIDE INDUSTRIES**CONTRACTS IN PROGRESS**

Contracts as of 08/02/2002

Start	Completion Date	Description	Price	Total Contract	Contract Billings to Date	Contract Costs to Date	Percent Incurred to Date	Completed	% Gross Profit to Date	Estimated Cost to Complete
Estimated Contract Date	Contract Number									
4/1/2002	4/1/2002	U.S. Customs -C.	1,000,000.00	2,000,000.00	1,000,000.00	1,000,000.00	100%	Completed	0.00%	1,000,000.00
7/23/2002	8/18/2002	DANEK-Mexico	1,000,000.00	1,000,000.00	1,000,000.00	1,000,000.00	100%	Completed	0.00%	1,000,000.00
4/14/2002	8/18/2002	Policia Fiscal	719,542.14	719,542.14	719,542.14	719,542.14	100%	Completed	0.00%	719,542.14
5/15/2002	8/14/2002	Ejercito de Colombia	975,000.00	975,000.00	73,865.00	73,865.00	7.55%	In Progress	438,750.00	438,750.00
3/20/2002	8/24/2002	DANEK-Mexico	236,186.37	236,186.37	236,186.37	236,186.37	100%	Completed	0.00%	236,186.37
4/17/2002	9/14/2002	U. S. Customs -C.	525,000.00	525,000.00	0.00	0.00	0.00%	In Progress	0.00%	525,000.00
4/24/2002	9/28/2002	USA PRHA Security Shelters	2,500,000.00	2,500,000.00	0.00	0.00	0.00%	In Progress	1,120,000.00	1,120,000.00

CONTRACTS IN PROGRESS

Contracts as of 08/02/2002		Description	Price	to Date	Incurred to Date	Completed	to Date	to Complete	Scheduled	E+F	Scheduled
Start	Completion Date										
11/27/2002	7/27/2003	Saudi Air Force Weapons of Mass Destruction Detection Platforms - Note 4	37,752,406.16	0	0	0	0	0	0	16,487,704.00	
2/11/2002	11/14/2002	EGYPTIAN PRESIDENTIAL GUARD - C-Weapons of Mass Destruction and COMJAM Platforms	27,900,612.60	0	0	0	0	0	0	11,716,257.28	
6/16/2002	11/18/2003	National Security Police - Ministry of Interior - Egypt - Note 3	572,572,610.00	0	0	0	0	0	0	234,029,044.00	
4/23/2002	9/12/2002	DISIP-Venezuela - Note 3	2,000,000.00	0	0	0	0	0	0	985,000.00	
3/20/2002	10/16/2002	DISIP-Venezuela - Note 3	13,600,000.00	0	0	0	0	0	0	6,440,000.00	
8/15/2002	3/31/2002	DOJ/FBP S.O.R.T. Trailers	338,320.60	0	0	0	0	0	0	138,000.00	
9/16/2002	6/30/2003	Ministry of Interior (MO) KSA - Command & Control Platforms (10ea)	6,459,940.00	0	0	0	0	0	0	2,829,975.00	
7/26/2002	10/30/2002	Ministry of Interior (MO) Ghana - EOD Platform (2ea)	490,000.00	0	0	0	0	0	0	170,000.00	
7/16/2002	12/31/2002	IDF - EOD Platform (10ea)	2,450,000.00	0	0	0	0	0	0	850,000.00	

Contract ID	Contract Name	Amount	Start Date	End Date	Status
7/15/2002	0/2/2003 Pakistan VVP System	45,000,000.00			Completed

Note:**Black = Signed Contracts**

Yellow = Contracts In Process of being Signed

Red = Contracts Pending Approval

Note 1 • Awaiting Funding from
U. S. Congress - Plan Colombia Presidential Approval Final Approval

Note 2 • Awaiting Presidential Approval

Note 3 • Awaiting Funding from
U. S. Congress - Plan Colombia Presidential Approval Final Approval

Note 4 • Awaiting
Final Contract Price is given as sales per month.

Note 5 • Awaiting Funding

Note 6 • Awaiting Award

Note 7 • This is a 5 year contract and the

PHOENIX WORLDWIDE INDUSTRIES
CONTRACTS IN PROGRESS

PHOENIX WORLDWIDE INDUSTRIES									
CONTRACTS IN PROGRESS									
Contract Date	Estimated Contract Start	Completion Date	Contract Number	Description	Price	Total Contract to Date	Contract Billings to Date	Verify to Invoices & A/R	Scheduled
Start	Completion Date	Contract Number	Description	Price	Total Contract to Date	Contract Billings to Date	Verify to Invoices & A/R	Scheduled	E-F
8/14/03	11/15/03	11/15/03	Policia Fiscal	719,542.14					319,875.00
7/15/03	12/4/03	12/4/03	Ejercito de Colombia	976,000.00					438,760.00
7/17/03	10/17/03	10/17/03	U.S. Customs -C-	525,000.00					
8/17/03	2/14/04	2/14/04	U. S. Customs -C-	525,000.00					295,000.00
8/27/03	7/27/04	7/27/04	Saudi Air Force Weapons of Mass Destruction Detection Platforms - Note 4	37,762,406.16					16,467,204.00
9/16/03	8/15/04	8/15/04	Egyptian Presidential Guard -C- Weapons of Mass Destruction and COMJAM Platforms	27,900,612.60					11,718,257.28

CONTRACTS IN PROGRESS

Contracts as of 02/24/2003		Verify to Invoice								
Contract Date	Estimated Contract	Contract Number/ Ministry of Interior-Egypt Note 3	Total Contract	Contract Billings	Contract Costs	Scheduled	E/F	% Gross Profit	Estimated Cost	Scheduled
5/12/03	12/18/04	National Security Police- Ministry of Interior-Egypt	572,572,610.00	0	0	0	0	60	234,029,044.00	
8/23/03	12/12/03	DISIP-Venezuela - Note 8	2,000,000.00	0	0	0	0	60	995,000.00	
8/20/03	2/16/04	DIM-Venezuela - Note 8	13,500,000.00	0	0	0	0	60	8,400,000.00	
8/15/03	3/31/04	DO/FBP S.O.R.T. Trailers	336,320.00	0	0	0	0	0	138,000.00	
9/15/03	6/30/04	Ministry of Interior (MO) KSA - Command & Control Platforms (10ea)	6,469,950.00	0	0	0	0	0	2,828,975.00	
7/25/03	10/30/03	Ministry of Interior (MO) Ghana - EOD Platform (2ea)	490,000.00	0	0	0	0	0	170,000.00	
7/15/03	12/31/03	IDF - EOD Platform ((sea))	2,450,000.00	0	0	0	0	0	850,000.00	
7/25/03	8/20/04	Pakistan VIP System	45,000,000.00	0	0	0	0	0	18,687,850.00	
7/15/03	11/15/03	Ministry of Interior (MO) KSA - Command & Control Platforms (10ea)	1,000,000.00	0	0	0	0	0	400,000.00	

Note:

Yellow = Contracts in Process of being Signed

Note 1 - Awaiting funding from
U. S. Congress - Plan Colombia Presidential Approval

Note 3 - Awaiting
Final Approval

Note 4 - Awaiting
Total Contract Price is
given as sales per
month.

Note 2 - Awaiting Presidential
Approval

Note 5 - Awaiting
Funding

Note 6 - Awaiting Award

EXHIBIT 3

954 4237769 P 01/01

Internal Revenue Service

Department of the Treasury

04/13/2004

Trust Communities, Inc.
Attn: ROBERT E. PUCH, CPA
Fax to: 202-347-4469

A Notice(s) of Federal Tax Lien was filed in DADE COUNTY, FL. for the tax liabilities listed below for: PHOENIX WORLDWIDE INDUSTRIES, INC., 10780 SW 190TH ST., MIAMI, FL. 33157.

Type of Tax	Tax Period	Identifying Number	Unpaid Balance	STATUTORY ADDITIONS TO DATE: 05/08/2004		
				Interest	Penalty	Total
940	12/31/1999	59-2375232	1,293.76	61.51	106.88	1,462.15
941	09/30/1998	59-2375232	17,950.89	727.69	0.00	18,678.58
941	03/31/1999	59-2375232	10,306.30	417.76	0.00	10,724.06
941	06/30/1999	59-2375232	43,853.97	3157.73	1139.00	48,150.70
941	03/31/2000	59-2375232	22,048.42	4774.02	0.00	26,822.44
941	06/30/2000	59-2375232	11,296.06	673.74	96.34	12,066.14
941	09/30/2000	59-2375232	32,770.92	1357.10	1910.14	36,038.16
941	06/30/2001	59-2375232	47,804.89	3261.37	4872.96	55,939.22
941	09/30/2001	59-2375232	12,305.04	498.81	0.00	12,803.85
941	12/31/2002	59-2375232	349.94	14.54	0.00	364.48
941	03/31/2003	59-2375232	4,866.01	216.71	0.00	5,082.72
941	06/30/2003	59-2375232	5,385.92	159.53	0.00	5,545.45

The amount needed to full pay all liabilities and release the lien is \$ 233,677.95. A Certificate of Release of Federal Tax Lien will be issued immediately only if payment is made by:

1. Cash; or
2. Certified or cashier's check; or
3. Treasurer's check drawn on a national / state bank or trust company; or
4. Money order.

If the payment is made in any other form, the release will be delayed for 30 days or until evidence is furnished that the funds have been transferred.

Please make payment payable to THE UNITED STATES TREASURY and send it to:
 INTERNAL REVENUE SERVICE, ATTN: LIEN UNIT, STOP 5720
 7850 S.W. 6TH COURT
 PLANTATION, FL. 33324

Signature, Lien Unit Manager

954-423-7796 -FR

Telephone Number



EXHIBIT 4

PHOENIX WORLDWIDE INDUSTRIES, INC.

FINANCIAL STATEMENTS

MARCH 31, 2004 AND 2003

EXHIBIT

4

PHOENIX WORLDWIDE INDUSTRIES, INC.

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Statements of Operations	3
Statements of Stockholders' Equity (Deficiency)	4
Statements of Cash Flows	5
Notes to Financial Statements	6-18



REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Stockholders
Phoenix Worldwide Industries, Inc.
Miami, Florida

We have audited the accompanying balance sheets of Phoenix Worldwide Industries, Inc. (the Company) as of March 31, 2004 and 2003, and the related statements of operations, stockholders' equity (deficiency) and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Phoenix Worldwide Industries, Inc. as of March 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

As more fully described in Note 2, the Company is subject to certain significant risks and uncertainties. The Company's plans with respect to these matters are also described in Note 2, and certain significant subsequent events related to these matters are described in Notes 14 and 15.

A handwritten signature in black ink that reads "Rachlin Cohen & Holtz LLP". The signature is written in a cursive style with some variations in letter height and slant.

Miami, Florida
June 11, 2004, except for Note 14, as to
which the date is November 15, 2004, and Note 15,
as to which the date is January 26, 2005

Rachlin Cohen & Holtz LLP

One Southeast Third Avenue ■ Tenth Floor ■ Miami, Florida 33131 ■ Phone 305.377.4228 ■ Fax 305.377.8331 ■ www.rachlin.com
An Independent Member of Baker Tilly International

MIAMI ■ FORT LAUDERDALE ■ WEST PALM BEACH ■ ATLANTA

PHOENIX WORLDWIDE INDUSTRIES, INC.

BALANCE SHEETS

MARCH 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
<u>ASSETS</u>		
(Substantially all pledged)		
Current Assets:		
Cash and cash equivalents	\$ 86,156	\$ 255,281
Accounts receivable, net of allowance for doubtful accounts of \$0 and \$371,775	226,923	950,372
Inventories	<u>1,558,649</u>	<u>1,202,538</u>
Total current assets	1,871,728	2,408,191
Property and Equipment, Net	2,907,706	2,779,180
Inventories, Noncurrent	1,152,845	-
Other Assets	3,232	18,843
Total assets	<u>\$ 5,935,511</u>	<u>\$ 5,206,214</u>
 <u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
Current Liabilities:		
Current portion of long-term debt	\$ -	\$ 288,000
Accounts payable and accrued liabilities	671,544	159,558
Accrued officer's compensation	848,000	1,008,000
Loans payable, officer/director/major stockholder	319,774	271,180
Total current liabilities	<u>1,839,318</u>	<u>1,726,738</u>
Long-Term Debt, Net of Current Portion	<u>1,170,467</u>	<u>1,666,374</u>
Commitments, Contingencies, Subsequent Events and Other Matters		
Stockholders' Equity:		
Common stock; 50,000,000 shares of \$.00005 par value authorized; 9,020,940 and 9,014,940 shares issued and outstanding, respectively	451	451
Additional paid-in capital	7,605,314	7,545,314
Deferred loan modification costs	(213,815)	(391,052)
Accumulated deficit	<u>(4,466,223)</u>	<u>(5,341,611)</u>
Total stockholders' equity	<u>2,925,726</u>	<u>1,813,102</u>
Total liabilities and stockholders' equity	<u>\$ 5,935,511</u>	<u>\$ 5,206,214</u>

See notes to financial statements.

PHOENIX WORLDWIDE INDUSTRIES, INC.

STATEMENTS OF OPERATIONS

YEARS ENDED MARCH 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
Revenues	\$ 5,463,433	\$ 2,965,064
Cost of Revenues	<u>2,680,366</u>	<u>1,436,290</u>
Gross Margin	<u>2,783,067</u>	<u>1,528,774</u>
Operating Expenses:		
Officers' compensation	231,437	224,400
Selling, general and administrative	<u>1,363,926</u>	<u>1,375,169</u>
	<u>1,595,363</u>	<u>1,599,569</u>
Income (Loss) from Operations	<u>1,187,704</u>	<u>(70,795)</u>
Other Income (Expense):		
Interest expense	(147,938)	(428,545)
Costs incurred in connection with loan financing, extensions and modifications of financing arrangements	(166,667)	(156,111)
Gain on forgiveness of debt	- 212,350	
Interest income	<u>2,289</u>	<u>2,407</u>
	<u>(312,316)</u>	<u>(369,899)</u>
Income (Loss) Before Income Taxes	875,388	(440,694)
Income Taxes	-----	-----
Net Income (Loss)	<u>\$ 875,388</u>	<u>\$ (440,694)</u>

See notes to financial statements.

PHOENIX WORLDWIDE INDUSTRIES, INC.

STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIENCY)

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Deferred Loan Modification Costs</u>	<u>Accumulated Deficit</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>			
Balance, March 31, 2002	8,461,140	\$ 423	\$ 4,655,175	\$ (45,000)	\$ (4,900,917) \$ (290,319)
Year Ended March 31, 2003:					
Shares issued in connection with private placement, net of expenses:					
Issued at \$5 per share	409,500	20	2,033,079	-	2,033,100
Issued at \$10 per share	21,300	1	212,999	-	213,000
Shares issued in connection with convertible debt	100,000	5	499,995	(500,000)	-
Shares issued in connection with conversion of debt to equity	19,000	1	94,999	-	95,000
Shares issued for services	4,000	-	20,000	-	20,000
Stock options granted in connection with convertible debt	-	-	29,067	(29,067)	-
Amortization of deferred loan modification costs	-	-	-	183,015	183,015
Net loss	-	-	-	(440,694)	(440,694)
Balance, March 31, 2003	9,014,940	451	7,545,314	(391,052)	(5,341,611) 1,813,102
Year Ended March 31, 2004:					
Shares issued in connection with private placement (\$10 per share)	6,000	-	60,000	-	60,000
Amortization of deferred loan modification costs	-	-	-	177,237	177,237
Net income	-	-	-	-	875,388 875,388
Balance, March 31, 2004	9,020,940	\$ 451	\$ 7,605,314	\$ (213,815)	\$ (4,466,223) \$ 2,925,726

See notes to financial statements.

PHOENIX WORLDWIDE INDUSTRIES, INC.

STATEMENTS OF CASH FLOWS

YEARS ENDED MARCH 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
Cash Flows from Operating Activities:		
Net income (loss)	\$ 875,388	\$ (440,694)
Adjustments to reconcile net income (loss) to net cash and cash equivalents provided by (used in) operating activities:		
Depreciation and amortization	522,730	527,072
Amortization of costs incurred in connection with loan financing, extensions and modifications of financing arrangements	166,667	156,111
Common stock issued for services rendered	-	20,000
Stock options granted in connection with convertible debt	10,570	4,404
Gain on forgiveness of debt	-	(212,350)
Change in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	723,449	(460,669)
Inventories	(1,508,956)	152,242
Other assets	15,611	(12,128)
Increase (decrease) in:		
Accounts payable and accrued liabilities	511,986	(243,922)
Accrued officer's compensation	<u>(160,000)</u>	<u>16,000</u>
Net cash and cash equivalents provided by (used in) operating activities	<u>1,157,445</u>	<u>(493,934)</u>
Cash Flows from Investing Activities:		
Purchases of property and equipment	<u>(651,257)</u>	<u>(673,321)</u>
Cash Flows from Financing Activities:		
Proceeds from issuances of common stock	60,000	2,106,100
Proceeds from long-term debt	-	2,346,366
Payments on long-term debt	(783,907)	(2,959,636)
Net proceeds (payments) on loans payable, officer/director/major stockholder	<u>48,594</u>	<u>(166,936)</u>
Net cash and cash equivalents provided by (used in) financing activities	<u>(675,313)</u>	<u>1,325,894</u>
Net Increase (Decrease) in Cash and Cash equivalents	<u>(169,125)</u>	<u>158,639</u>
Cash and Cash equivalents, Beginning	<u>255,281</u>	<u>96,642</u>
Cash and Cash equivalents, Ending	<u>\$ 86,156</u>	<u>\$ 255,281</u>
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the year for interest	<u>\$ 137,368</u>	<u>\$ 428,545</u>
Noncash Financing Activities:		
Deferred financing costs resulting from shares issued in connection with debt	<u>\$ -</u>	<u>\$ 391,052</u>
Conversion of debt to equity	<u>\$ -</u>	<u>\$ 95,000</u>

See notes to financial statements.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2004 AND 2003

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business

Phoenix Worldwide Industries, Inc., (the Company) designs, manufactures, equips, and assembles all types of forensic vehicles (including mobile intelligence platforms, mobile crime laboratories, mobile surveillance platforms, SWAT, counter assault anti-terrorism platforms, mobile explosives detection platforms, mobile border detection and interdiction platforms, dignitary protection platforms and equipment, psychological operational and C3I vehicles), electronic counter measures (ECM), electronic counter-counter measures (ECCM), electronic passive measures (EPM), air dropped and man emplaced unattended sensors and psychological operations equipment, psychological warfare and perception management equipment.

Revenue Recognition

The Company recognizes revenue when the contract is completed for contracted jobs and when the product is shipped for other sales. Contracts that require services to be provided over a period of time are recognized as revenue as the services are provided. Payments received in advance of the services provided are reported as deferred revenue in the accompanying balance sheet.

For government "Cost-Plus-Fixed-Fee" contracts with a term greater than six months, the Company recognizes revenue when the client is billed under the terms of the contract.

Inventories

Inventories are stated at the lower of cost (specific identification method) or market. The Company determines market as estimated net realizable value or current replacement cost of inventories.

The Company has classified inventories not reasonably expected to be consumed in its production process or contract business within the Company's normal operating cycle, based upon historical experience, as a noncurrent asset in the accompanying balance sheet.

Property and Equipment

Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the assets. Gain or loss on disposition of assets is recognized currently. Repairs and maintenance are charged to expense as incurred. Major replacements and betterments are capitalized and depreciated over the remaining useful lives of the assets.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's knowledge of current events and actions it may undertake in the future, they may ultimately differ from actual results.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Income Taxes

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, which requires the use of the liability method of accounting for income taxes. Deferred income taxes are provided for temporary differences between financial statement and income tax reporting, principally from the use of accelerated depreciation methods for income tax purposes, accrued stockholder's compensation and net operating loss carryforwards.

Concentration of Credit Risk

Cash and Cash Equivalents

The Company maintains deposit balances at financial institutions that, from time to time, may exceed federally insured limits. At March 31, 2004, there were no deposit balances in excess of federally insured limits. The Company maintains its cash with high quality financial institutions, which the Company believes limits this risk.

In addition, the Company maintains funds in money market accounts with financial institutions that are not insured by the FDIC. These funds, which are invested primarily in money market mutual funds at March 31, 2004, may be subject to insurance by SIPC, Securities Investor Protection Corporation, subject to various limitations. At March 31, 2004, a total of approximately \$51,000 was held in these accounts.

Accounts Receivable

Substantially all of the Company's accounts receivables are due from federal, state, local and foreign governmental agencies. Accordingly, management believes substantially all accounts receivables from these agencies are collectible.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Concentration of Credit Risk (Continued)

Accounts Receivable (Continued)

With regard to non-governmental customers, the Company does business and extends credit based on an evaluation of the customers' financial condition generally without requiring collateral. Exposure to losses on receivables is expected to vary by customer due to the financial condition of each customer. The Company monitors exposure to credit losses and maintains allowances for anticipated losses when necessary under the circumstances.

Delinquent accounts receivable are charged against the allowance for doubtful accounts once uncollectibility has been determined. Accounts receivable are considered to be past due and placed on delinquent status based on contractual terms, as well as how frequently payments are received, on an individual account basis.

Software Development Costs

In accordance with the criteria set forth in Statement of Financial Accounting Standards ("SFAS") No. 86, "Accounting for the Cost of Computer Software to be Sold, Leased or Otherwise Marketed," development costs incurred in the research and development of new software products are expensed as incurred until technological feasibility in the form of a working model has been established, at which time such costs are capitalized, subject to recoverability. The Company capitalized approximately \$247,000 in software development costs for the year ended March 31, 2004.

NOTE 2. SUMMARY OF SIGNIFICANT RISKS AND UNCERTAINTIES

Tax Lien Arising from Disputed Payroll Tax Liabilities

On February 4, 2004, the Internal Revenue Service (IRS) placed a federal tax lien on the Company's assets, asserting that the Company had approximately \$210,000 of unpaid payroll taxes, including assessed penalties and interest, relating to quarterly periods from September 1998 to June 2003. Based upon a detailed review of the Company's financial records, management believed that all of the payroll taxes for the periods in question had been paid, although certain payments made were delinquent. In its review, management has determined that a number of payments made were not done in the manner or with the appropriate documentation prescribed by the IRS and, therefore, these payments were either not applied or misapplied by the IRS. The Company had been attempting to resolve these differences with representatives of the IRS; however, these efforts were not successful and, on February 4, 2004, the IRS imposed the tax lien.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

(Continued)

NOTE 2. SUMMARY OF SIGNIFICANT RISKS AND UNCERTAINTIES (Continued)

Tax Lien Arising from Disputed Payroll Tax Liabilities (Continued)

In May, 2004, an appeals conference was held between representatives of the Company and an IRS Appellate Officer. At that conference, the Company presented documentation to the Appellate Officer in support of the Company's contention that the payroll taxes had been paid and the assessments were improper. The IRS indicated that substantially all of the assessments in question should be abated, and the matter was sent to the Collections Division of the IRS for processing. Although it may take several months for this process to be completed, management believes that any remaining liability should be immaterial and will be paid by the Company immediately, and any refund due because of certain good faith payments that had been made by the Company should be issued immediately. The lien that has been placed on the assets of the Company by the IRS remains in place until all of the abatements have been processed and the quarterly payroll liability accounts cleared.

See Note 14 regarding subsequent events relating to payment of the remaining balance of the disputed payroll tax liabilities and the release of the federal tax lien.

Real Estate Mortgage Foreclosure Action

The holder of the secured convertible note payable has brought a real estate mortgage foreclosure action on the note, to foreclose on personal property and on a personal guaranty action, seeking the unpaid principal sum of \$1,170,467, default interest and attorneys' fees and costs of litigation. The action is based on a claimed modification to the promissory note.

An answer, affirmative defenses and demand for jury trial have been filed on behalf of the Company. All parties are in the process of obtaining discovery in this case. A motion for summary judgment was served and a hearing is set for December 2004.

The Company has asserted defenses that the purported modification of the note is not valid; the Company has otherwise fully performed under the terms of the note and mortgage; and the Company believes that there is no merit to the claim.

The premise underlying the plaintiff's claim of default is that, as the result of a letter and an email dated July 28, 2003 and performance by the Company afterwards, there was a binding modification of the original note. According to the plaintiff, the Company defaulted under the mortgage and original note, as purportedly modified, when the Company failed to make a balloon payment of \$500,000 on December 15, 2003 and failed to pay the balance of the note on September 15, 2004. The Company prepaid a portion of the principal balance of the original note, making such prepayment voluntarily in accordance with the terms of the original note, which permits prepayments of principal at the discretion of the Company. In this pending case, the Company's position is that it merely offered to prepay a portion of the original note, not to modify it.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 2. SUMMARY OF SIGNIFICANT RISKS AND UNCERTAINTIES (Continued)

Real Estate Mortgage Foreclosure Action (Continued)

In the opinion of management, based upon advice of counsel, the Company believes that it will be able to defend this action successfully. If the Company prevails, then it will be entitled to reasonable attorneys' fees and costs. However, should the plaintiff prevail, then the Company would be liable for the principal and interest of the original note, as modified, together with reasonable attorneys' fees and costs.

See Note 15 regarding subsequent settlement agreement relating to the real estate mortgage foreclosure action and subsequent financing. Based upon the subsequent refinancing of this debt, the Company has presented the obligation related to the secured convertible note payable as a long-term liability in accordance with the terms of the original note in the accompanying historical balance sheet at March 31, 2004.

Stockholder Litigation

In July 2004, certain stockholders of the Company filed suit against the Company, its President and Chief Executive Officer and the Company's auditor claiming that the Company violated Section 10(b) of the Securities Exchange Act of 1934, and Regulation 10b-5 promulgated thereunder by the Securities and Exchange Commission.

In this complaint, the plaintiffs do not assert what amounts of damages have been suffered. Plaintiffs claim that the Company misrepresented the contracts it had with customers and failed to disclose that there was a controversy with the IRS over unpaid employment taxes. Plaintiffs also sued under District of Columbia common law of fraud and negligent misrepresentation. The plaintiffs sued the Company's auditor for negligence in failing to address adequately the unpaid employment tax issue in the Company's financial statements.

See Note 14 regarding subsequent events relating to payment of the remaining balance of payroll tax liabilities and the release of the federal tax lien.

In response to the complaint, the Company has filed a motion to dismiss based on a number of pleading problems and inconsistencies in the allegations of misrepresentation. The Company believes that plaintiffs' claims against the Company under Section 10(b) and Rule 10(b)5 should fail because the alleged misrepresentations are contradicted or unsupported by the claimed documentary corroboration; plaintiffs have failed to plead sufficient facts establishing reasonable reliance; plaintiffs have failed to plead scienter with the statutory particularity required; plaintiffs have failed to plead the facts and claims underlying the fraud with the required specificity; and, plaintiffs have failed to plead causation.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

(Continued)

NOTE 2. SUMMARY OF SIGNIFICANT RISKS AND UNCERTAINTIES (Continued)

Stockholder Litigation (Continued)

The Company has aggressively defended this claim, which it believes to be both meritless and an effort by plaintiffs' investors to obtain a short-term return of their investment, which, by its nature, is supposed to be long-term. The motion to dismiss made by the Company is still pending before the court.

The Company believes, based upon advice of counsel, that plaintiffs will have a difficult time of overcoming the motion to dismiss, particularly as they have contradicted the claimed misrepresentations internally in their complaint. Further, the financial statements of the Company for the relevant period contain notes to the financial statements advising of the pending employment tax issues between the Company and the IRS. Accordingly, the Company believes that the dismissal of the complaint by the court is more likely than not. However, it is not entirely predictable whether the court will again permit plaintiffs to amend their complaint.

If the court grants the motion to dismiss, and does not permit plaintiffs to amend their complaint once again, then the likelihood of an unfavorable outcome for the Company is remote. While the Company does not believe the plaintiffs will be able to successfully amend their complaint, it remains a possibility. Accordingly, if plaintiffs are unable to amend their claim to properly state their allegations and overcome the inconsistencies of the original complaint, then the Company believes that there is a reasonable likelihood of dismissal by the court and the award of reasonable attorneys' fees and costs to the Company.

Based upon its evaluation of this matter, together with the advice of counsel, the Company has presented the aggregate amount of equity funds it received from the plaintiffs (\$1,099,500) as a component of stockholders' equity in the accompanying historical balance sheet at March 31, 2004.

As an alternative presentation, the Company has set forth below a pro forma assumed condensed presentation of what the Company's financial position would have been at March 31, 2004 assuming that the plaintiffs were able to amend their complaint and were to prevail on the notion that their investments were subject to rescission.

Pro Forma Assumed Presentation

The following pro forma assumed condensed balance sheet presents the effects of what the Company's financial position would have been at March 31, 2004 under the following assumptions, as more fully described above:

1. Classification of the proceeds received from plaintiff stockholders as common stock subject to potential rescission.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

(Continued)

NOTE 2. SUMMARY OF SIGNIFICANT RISKS AND UNCERTAINTIES (Continued)

Pro Forma Assumed Presentation (Continued)

	<u>As Reported</u>	<u>Pro Forma Assumed Adjustments</u>	<u>Pro Forma Assumed As Adjusted</u>
Current assets	\$ 1,871,728	\$ -	\$ 1,871,728
Other assets	4,063,783	-	4,063,783
Total assets	<u>\$ 5,935,511</u>	<u>\$ -</u>	<u>\$ 5,935,511</u>
Current liabilities	\$ 1,839,318	\$ -	\$ 1,839,318
Long-term debt	1,170,467	-	1,170,467
Common stock subject to potential rescission	- 1,099,500	(1)	1,099,500
Stockholders' equity	<u>2,925,726</u>	<u>(1,099,500)</u> (1)	<u>1,826,226</u>
Total liabilities and stockholders' equity	<u>\$ 5,935,511</u>	<u>\$ -</u>	<u>\$ 5,935,511</u>

NOTE 3. CONCENTRATIONS

Major Customers

The Company's sales are made primarily to customers who are comprised of federal, state, local, and foreign governmental agencies, as follows:

<u>Customer</u>	2004		<u>Customer</u>	2003	
	<u>Revenue</u>	<u>%</u>		<u>Revenue</u>	<u>%</u>
1	\$2,361,000	43	1	\$1,617,000	55
2	2,171,000	39	2	902,000	30
3	939,000	17	3	396,000	13

NOTE 4. INVENTORIES

	<u>2004</u>	<u>2003</u>
Current:		
Raw materials	\$ 49,079	\$ 100,317
Work in process	233,148	-
Finished goods	<u>1,276,422</u>	<u>1,102,221</u>
	<u>\$ 1,558,649</u>	<u>\$ 1,202,538</u>

PHOENIX WORLDWIDE INDUSTRIES, INC.NOTES TO FINANCIAL STATEMENTS
(Continued)**NOTE 7. DEBT**

On July 24, 2002, the Company's lender (the "Former Lender") assigned all three promissory notes due them (see below) to a new lender (the "New Lender") which directly purchased the notes. The Company and the New Lender entered into an agreement whereby the New Lender consolidated the three notes into one secured convertible note for \$2,000,000. Principal and accrued interest is payable monthly in an amount equal to 5% of gross revenues, net of returns, allowances and commissions. Commencing in October 2003, the Company voluntarily increased the monthly payments to an amount equal to 10% of gross revenues. This note bears interest at a fixed rate of 7% per annum and matures in July 2005. As provided for in the terms of the convertible note, the Company further granted an option to the New Lender to purchase 100,000 shares of common stock since the Company did not obtain a new mortgage loan on its real property within 90 days as required under the agreement (see Note 10). The agreement provides for the conversion of the outstanding loan into common shares based on a conversion price of \$5.01, \$6.01 and \$7.01, on the first, second and third anniversary of the loan, respectively. The Company has the right to prepay the note without penalty prior to maturity; in the event the Company does repay any of this note, the convertibility rights under the note with respect to the prepaid portion shall be detachable as a warrant for the purchase of common stock consistent with the convertibility terms described above. As an inducement to the New Lender, the Company had originally issued to the New Lender warrants to purchase up to 400,000 shares. In exchange for these warrants, the Company subsequently issued the New Lender an additional 100,000 shares which was valued at \$500,000; this amount is being amortized over the life of the note and the unamortized balance of the deferred loan modification costs is presented as a reduction of stockholders' equity. The balance of the secured convertible note was \$1,170,467 and \$1,954,374 as of March 31, 2004 and 2003 respectively.

The holder of the secured convertible note payable has brought a real estate mortgage foreclosure action on the note, to foreclose on personal property and on a personal guaranty action, seeking the unpaid principal sum of \$1,170,467, default interest and attorneys' fees and costs of litigation. See Notes 2 and 15.

In 2003, the amount presented as the current portion of long-term debt represents management's best estimate of amounts expected to be paid currently based on the applicable percentages of projected net revenues for the ensuing year. In 2004, based upon the subsequent refinancing of this debt (see Note 15), the Company has presented this obligation as long-term debt.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

(Continued)

NOTE 8. COSTS IN CONNECTION WITH LOAN FINANCING, EXTENSIONS AND MODIFICATIONS OF FINANCING ARRANGEMENTS

2004 2003

In July 2002, the Company and a new lender entered into a new, secured convertible note agreement for \$2,000,000 (see Note 7). As an inducement to the lender, the Company granted the New Lender a warrant, as described above, to purchase up to 400,000 shares of the Company's shares. The Company subsequently, in exchange for the warrants, issued an additional 100,000 shares valued at \$500,000 to the New Lender. The amount is being amortized over the life of the note as costs incurred in connection with loan financing, extensions and modifications of financing arrangements and the unamortized balance of the deferred loan modification costs is presented as a reduction of stockholders' equity.

\$ 166,667 \$ 111,111

Other	45,000
	<u>\$ 166,667</u>
	<u>\$ 156,111</u>

NOTE 9. RELATED PARTY TRANSACTIONS

Officers' Compensation

The Company has accrued an annual compensation expense of \$144,000 for the Company's President (who is also a major stockholder and director) from March 31, 1996 through March 31, 2003. During 2003, the President's annual compensation was increased to \$192,000. The Company paid the President \$352,000 during the year ended March 31, 2004 with the excess of \$160,000 recorded as a reduction of the accrued officer's compensation. Additionally, during the year ended March 31, 2004, the Company paid the Vice President an annual compensation of approximately \$39,400. As of March 31, 2004 and 2003, accrued officer's compensation amounted to \$848,000 and \$1,008,000, respectively, due to the Company's President.

Professional Fees

During 2004, the Company paid approximately \$42,000 to certain directors to reimburse them for expenses incurred and other services rendered for the benefit of the Company.

Loans Payable, Officer/Director/Major Stockholder

The Company's President, who is also a director and major stockholder, from time to time provides working capital loans to the Company. The loans are unsecured and call for interest payments at 15% per annum. Principal and interest payments on these loans are due on demand. As of March 31, 2004 and 2003, these loans amounted to \$319,774 and \$271,180, respectively.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS

(Continued)

NOTE 9. RELATED PARTY TRANSACTIONS (Continued)

Stockholder's Loan Payable

In October 2001, a stockholder loaned the Company \$225,000, which was convertible into 45,000 shares of the Company's common stock at \$5 per share. During the year ended March 31, 2002, the Company repaid the stockholder \$130,000. During the year ended March 31, 2003, the stockholder converted the remaining outstanding balance of this loan (\$95,000) into 19,000 shares of the Company's common stock (see Note 10).

NOTE 10. EQUITY TRANSACTIONS

In July 2002, the Company issued 100,000 shares of common stock valued at \$500,000 to a new lender as an inducement for the lender to grant the loan (see Note 7).

In July 2002, the Company entered into a loan agreement with a new lender (see Note 7). As part of this agreement, the Company granted the Lender an option to purchase up to 100,000 shares of the Company's common stock at \$5.01, \$6.01 and \$7.01, on the first, second and third anniversary of the loan, respectively. The fair value of the options issued under this agreement was estimated to be approximately \$29,000 based upon a financial analysis of the terms of the options using the Black-Scholes Pricing Model with the following assumptions: expected volatility 0%; a risk free interest rate of 2.25% and an expected holding period of three years. This amount is being amortized to interest expense over the term of the loan.

In August 2002, the Company issued 4,000 shares of the Company's common stock valued at \$20,000 as compensation for professional services rendered.

In September 2002, a stockholder converted all remaining convertible debt of \$95,000 into 19,000 shares of the Company's common stock (see Note 9).

NOTE 11. PRIVATE PLACEMENT OFFERING

On August 1, 2001, the Company issued a Private Placement Offering Memorandum (the Offering) to sell 2,000,000 shares of common stock (the Shares) at \$5 per share, provided that the Company may, in the event of additional investor demand, offer up to 3,000,000 shares. Investors who purchased Shares in the Offering were required to make a minimum investment of \$50,000 for the purchase of 10,000 shares subject to the discretion of Management to accept less on a situation specific basis. This Offering was submitted to prospective investors on a confidential basis for use solely in connection with a private placement offering under Rule 506 of Regulation D promulgated under the Securities Act of 1933 and pursuant to Section 4(2) of the Act. The Offering was to remain open until all shares authorized to be issued were purchased.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 11. PRIVATE PLACEMENT OFFERING (Continued)

In September 2002, the Board of Directors authorized and increased the offering price of common stock from \$5 per share to \$10 per share, for all shares purchased pursuant to the Offering. An addendum to the Private Placement Offering Memorandum, effective September 2, 2002, was issued disclosing this change in price and other developments. During fiscal 2004, the Company sold 6,000 shares for \$60,000 in connection with the Offering. As of March 31, 2004, the Company had issued a total of 677,940 shares under this Offering.

NOTE 12. KEY-MAN LIFE INSURANCE

The Company maintains \$7,750,000 in life insurance policies on its president, who is also a major stockholder and director.

NOTE 13. INCOME TAXES

The net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes are reflected in deferred income taxes. Significant components of the Company's current deferred tax assets and liabilities are as follows:

	<u>2004</u>	<u>2003</u>
Long-Term Deferred Tax Assets:		
Net operating loss carryforward	\$ 1,315,000	\$ 1,791,000
Officer's compensation	<u>319,000</u>	<u>398,000</u>
Total long-term deferred tax assets	1,634,000	2,189,000
Valuation allowance	<u>(1,487,000)</u>	<u>(2,160,000)</u>
	147,000	29,000
Long-Term Deferred Tax Liabilities:		
Depreciation	<u>(147,000)</u>	<u>(29,000)</u>
Net long-term deferred tax asset (liability)	<u>\$ -</u>	<u>\$ -</u>

The Company has net operating loss carryforwards for federal income tax purposes as of March 31, 2004 of approximately \$3,617,000, after having utilized approximately \$819,000 to offset taxable income in the year ended March 31, 2004. The net operating losses are available to offset future federal taxable income, if any, through 2023.

PHOENIX WORLDWIDE INDUSTRIES, INC.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 14. SUBSEQUENT EVENTS

On November 15, 2004, after numerous discussions with the Collections Division of the IRS subsequent to the appeals conference held in May 2004, the Company paid the IRS the remaining liability for the disputed payroll tax liabilities in the amount of \$16,468 in order to obtain a release of the \$210,110 federal tax lien (see Note 2). The Company is continuing in its efforts to obtain a refund of the amount paid. On that same date, the IRS issued a Certificate of Release of Federal Tax Lien in that amount of \$210,110, which the Company had recorded in the appropriate county records.

See Note 2, Real Estate Mortgage Foreclosure Action and Stockholder Litigation, and Note 15 regarding developments relating to these matters that occurred subsequent to March 31, 2004.

NOTE 15. SETTLEMENT AGREEMENT RELATING TO REAL ESTATE FORECLOSURE ACTION AND SUBSEQUENT FINANCING

On January 26, 2005, the Company entered into a Limited General Mutual Release and Settlement Agreement relating to the pending real estate foreclosure action (see Note 2) and another complaint filed by Mr. Jay Zawatsky, a director, on November 19, 2004. Under the terms of this agreement, the holder of the mortgage, Trust Communities, Inc., and the Company released each other from all claims which have arisen out of the actions; Trust Communities dismissed the actions with prejudice, with each side bearing its own costs, and canceled the promissory note and released the mortgage securing the debt; Mr. Jay Zawatsky, a plaintiff in one of the actions, resigned his membership from the Company's Board of Directors; and Trust Communities agreed to cancel and return the 500,000 detachable warrants for the purchase of Company shares which was the subject of the Trust Communities action. In exchange, the Company paid Trust Communities approximately \$1,170,000 in principal, \$71,000 in interest, and \$55,000 in additional consideration, for a total of approximately \$1,296,000.

Additionally, on January 26, 2005, the Company executed a balloon mortgage and promissory note with a new lender in the principal amount of \$1,500,000. The note provides for interest at 12% per annum, payable interest only on a monthly basis commencing March 1, 2005 until February 1, 2006, at which time the remaining principal balance is due. If within the first six months of the term of the note, the Company makes prepayments exceeding 20% of the original principal amount of the note, the note provides for a prepayment penalty in an amount equal to six months of advance interest on the original note amount. The Company has pledged its real estate as collateral for the mortgage and note, and the Company's officer/director/major stockholder co-signed the mortgage and note.

**IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA**

PAUL I. BURMAN, <i>et. al.</i> Plaintiffs, v. PHOENIX WORLDWIDE INDUSTRIES, INC., <i>et. al.</i> Defendants.	$)$ $)$ $)$ $)$ $)$ $)$ $)$ $)$ $)$ $)$ $)$ $)$	Case No. 1:04CV1276 The Hon. Reggie Walton
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SECOND AMENDED COMPLAINT

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Plaintiffs, PAUL I. BURMAN (hereinafter “Burman”), ROBERT C.WARRINER (“Warriner”), SYLVIA J. ROLINSKI (“Rolinski”), and INGERSOLL & BLOCH, Chartered Employees Profit Sharing Plan and Trust, by and through its trustees William B. Ingersoll and Stuart Marshall Bloch (“I&B”, collectively with Burman, Warriner and Rolinski , “Plaintiffs”), by and through undersigned counsel, and pursuant to F.R.Civ.P. 7, 8, 9 and 15 and this Court’s Order entered August 30, 2005 bring this
Second Amended Complaint against Defendants PHOENIX WORLDWIDE
INDUSTRIES, INC. (“Phoenix”), DR. J. AL ESQUIVEL SHULER (“Shuler,” collectively with Phoenix the “Phoenix Defendants”), and the accounting firm of RACHLIN, COHEN & HOLTZ, LLP (“R&C,” collectively with the Phoenix Defendants, the “Defendants”) for statutory securities fraud, common law fraud and

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misrepresentation, negligent misrepresentation, breach of fiduciary duty and negligence, and state and aver as follows:¹

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INTRODUCTION

This case arises out of the misrepresentations – both express and by omission – made by the Phoenix Defendants to induce the Plaintiffs to invest in Phoenix. The Phoenix Defendants then reiterated the misrepresentations, failed to correct the misrepresentations, and failed to correct the omissions, in order to induce some of the Plaintiffs to invest additional sums in Phoenix.

Plaintiffs' Phoenix investment decisions were not the result of their lack of diligence, or of misunderstanding. To the contrary, Plaintiffs repeatedly sought from the Phoenix Defendants specific answers to material questions. Given the opportunity to correct or explain their misstatements, the Phoenix Defendants again chose outright and actionable deception.

As a direct and foreseeable consequence of the Phoenix misconduct, and the concomitant negligence of R&C, Plaintiffs were wrongly induced to invest \$1,116,500 in Phoenix.

PARTIES

Plaintiffs

1. Plaintiff Burman is an individual residing in the State of Maryland, who does, engages in and transacts business in the District of Columbia, including business out of which these claims arise. Plaintiff Burman is 87 years old. Between September 25, 2001

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¹ Plaintiffs preserve for purposes of appeal certain "allegations of failure to secure revenue." See Order at 31 and see First Amended Complaint, Count IV (Breach of Fiduciary Duty) at paragraphs 129-132, and the last clause of paragraph 133. Those claims were dismissed. Order, at 31.

and September 1, 2002, Plaintiff Burman purchased 61,400 shares of Phoenix for \$307,000.

2. Plaintiff Warriner is an individual residing in the State of Maryland, who does, engages in and transacts business in the District of Columbia, including business out of which these claims arise. On August 27, 2002, Plaintiff Warriner purchased 5,000 shares of Phoenix for \$25,000.

3. Plaintiff Rolinski is an individual residing in the State of Maryland. Between February 20, 2002 and January 15, 2003, Plaintiff Rolinski purchased 4,900 shares of Phoenix for \$34,400.

4. Plaintiff I&B is an employee profit sharing plan and trust located in the District of Columbia and doing business in the District of Columbia, including business out of which these claims arise. Jay Zawatsky ("Zawatsky") is an investment manager of I&B. William B. Ingersoll and Stuart Marshall Bloch are the trustees of I&B. Between May 28, 2002 and July 22, 2002, Plaintiff I&B purchased 150,000 shares of Phoenix for \$750,000.

In addition, on or about July 22, 2002, Trust Communities, Inc., of which Zawatsky is the president, loaned to Phoenix in a secured transaction the sum of \$2,000,000. Phoenix defaulted on that debt, and Trust Communities, Inc. accelerated the note evidencing the debt and initiated foreclosure proceedings in Miami, Florida. Subsequent thereto, Phoenix refinanced and satisfied the Trust Communities, Inc. loan.

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Defendants

5. Defendant Phoenix is a corporation that has its principal place of business in the State of Florida. Phoenix solicited investments in the District of Columbia and

elsewhere. Phoenix manufactures and distributes, among other products and services, electronic systems for use in counter-terrorism and drug interdiction.

6. Defendant Shuler is an individual who, upon information and belief, resides in the State of Florida. Shuler is the founder of Phoenix . Shuler is, and at all times pertinent to the allegations in the Second Amended Complaint was, the president, chief executive officer, chairman of the board of directors, and majority stockholder of Phoenix. As of August 1, 2001, Shuler owned 76.88% of the outstanding stock of Phoenix. At the conclusion of the offering through which Plaintiffs invested, Shuler owned in excess of 60% of the outstanding shares of Phoenix. Shuler made material misrepresentations individually and on behalf of Phoenix to the Plaintiffs in the District of Columbia and elsewhere. In addition, Shuler, individually and on behalf of Phoenix, omitted to state facts that were material to the decisions of the Plaintiffs to participate in the offering of Phoenix securities.

Shuler was, and explicitly held himself out to be, privy to all material confidential and proprietary information concerning Phoenix, its operations, finances, financial condition, and present and future business prospects. Because of his possession of such information, Defendant Shuler knew of and recklessly disregarded the material misrepresentations made to Plaintiffs in connection with Plaintiffs' purchase of Phoenix securities and that material facts, which would have influenced the decisions of Plaintiffs to participate in the offering of Phoenix securities, were omitted from the securities offering materials and oral presentations to the Plaintiffs.

Defendant Shuler is liable as a direct participant in the wrongs complained of herein. In addition, Shuler, by reason of his status as chief executive officer and

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chairman of the board of directors, is a “controlling person” within the meaning of Section 20 of the Exchange Act and had the power and influence to cause Phoenix to engage in the unlawful conduct complained of herein. Because of his position of control, the individual Defendant was able to and did directly, or indirectly, control the conduct of Phoenix and its agents. To the extent that Shuler personally performed that wrongful act, he is directly liable. To the extent that other persons - for whose action Shuler, as a controllingg person is liable – perfomed the wrongful act, Shuler is liable as a controlling person.

Defendant Shuler controls the Phoenix Board of Directors by virtue of his offices, his equity holdings, and his personal or family relationships with the majority of the members of the Board of Directors.

Defendant Shuler is an insider of Phoenix and is an unsecured creditor of Phoenix. At all times pertinent to the allegations of the Second Amended Complaint, Shuler was owed, or claims to have been owed by Phoenix, accrued salary or benefits of no less than \$432,000 as of August 2001. That obligation was carried on Phoenix's books at an annual salary of \$144,000. As of March 31, 2003, according to Phoenix, “there are accruals of “\$1,008,000 and \$992,000” for “2003 and 2002” due to Shuler from Phoenix.

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7. Defendant R&C is a public accounting firm that, upon information and belief, has its principal place of business in Miami, Florida. R&C prepared the audited financial statements of Phoenix. The audited financial statements were presented to and relied upon by the Defendants in Washington, D.C. and elsewhere.

R&C held itself out to Plaintiffs as an agent of Phoenix. Phoenix identified R&C as its accounting firm and agent.

Agency Relationships

8. Defendant Shuler, by virtue of his positions, offices and statements as described in paragraph 6 above, is and at all times pertinent to the allegations of the ~~Second Amended Complaint was an agent for Phoenix.~~

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9. Defendant R&C, by virtue of the relationship and the statements described in paragraph 7 above, is and at all times pertinent to the allegations of the ~~Second Amended Complaint was an agent for Phoenix for accounting matters.~~

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10. Charles Levy ("Levy") is, and at all times pertinent to the allegations of the ~~Second Amended Complaint was, both a director and shareholder of Phoenix. Over the same period, Levy was and is the Chairman of Phoenix's Finance Committee. Levy was held out by the Phoenix Defendants as the Phoenix spokesperson, agent and representative for purchase and sale of Phoenix securities. Levy, by virtue of the offices and the statements described in this paragraph, is, and at all times pertinent to the allegations of the Second Amended Complaint was, the agent for Phoenix on matters related to the purchase and sale of Phoenix securities.~~

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JURISDICTION

Subject Matter Jurisdiction

11. This Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. §§ 1331, 1337, and Section 27 of the Securities and Exchange Act. Further, this action arises under Sections 10(b) and 20(a) of the Securities and Exchange Act (15 U.S.C. §§ 78j(6) and 78t(a)), Rule 10b-5 promulgated thereunder (17 C.F.R. § 240.10b-

5). In connection with the acts and omissions alleged in this Complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, mails and interstate telephone and Internet communications.

12. This Court has supplemental jurisdiction pursuant to 28 U.S.C. §1367. In addition, this court has jurisdiction pursuant to 28 U.S.C. § 1332. The amount in controversy as to each Plaintiff exceeds \$75,000, exclusive of interest and costs.

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Personal Jurisdiction

13. Defendants have significant personal contacts with the District of Columbia in accordance with the District of Columbia Long Arm Statute, including, but not limited to, D.C. Code § 13-423 (a) (1), (2), (3), (4). Therefore, the Defendants are subject to the personal jurisdiction of this Court. The causes of action asserted herein arise largely from Defendants' activities within the District of Columbia.

VENUE

14. Venue is proper in this Court pursuant to 28 U.S.C. § 1391(b).

FACTS COMMON TO ALL COUNTS

15 . Plaintiffs adopt and incorporate herein by reference as if specifically set forth herein the averments of paragraphs one through fourteen of the Second Amended Complaint.

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16. As is more fully set forth below, the Phoenix Defendants, from August 2001 through January 2003, consistently, repeatedly, knowingly and falsely, represented to Plaintiffs orally and in writing that Phoenix had obtained specific, large scale and enforceable contracts for the sale of Phoenix products (the " Contract

Misrepresentations"). Phoenix failed to correct the Contract Misrepresentations before purchase by Plaintiffs of Phoenix securities.

17. As is more fully set forth below, the Phoenix Defendants, from August 2001 to April, 2004, knowingly and with intent to deceive, failed to disclose to Plaintiffs that Phoenix had been, and continued to be, subject to substantial Internal Revenue Service ("IRS") tax deficiencies (the "IRS Misrepresentations"). Thereafter, Phoenix failed to correct the IRS Misrepresentations, and, when affirmatively questioned by Plaintiffs on the existence of any IRS tax deficiencies, falsely denied the existence of IRS tax deficiencies.

18. As is more fully set forth below, Plaintiffs and each of them relied on the Contract Misrepresentations, and relied on the IRS Misrepresentations, for purposes of electing to purchase Phoenix securities, and that reliance was reasonable under all of the facts and circumstances. As a direct and foreseeable consequence thereof, Plaintiffs sustained monetary damage in the amount of the sums paid for purchase of the securities, as set forth below and in paragraphs one through four of the ~~Second Amended~~ Complaint.

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As is more fully set forth below, defendant R&C failed to satisfy the applicable standard of care with regard to identification and disclosure of the IRS tax deficiencies.

Phoenix in 2001

19. In 2001 Shuler, Shuler's wife, Shuler's brother, and Levy were members of the board of directors and constituted a majority of the board.

20. On August 1, 2001, Phoenix issued a Private Placement Offering Memorandum (the "PPM") to sell 2,000,000 shares of Phoenix common stock. The

stock was to be offered to "accredited investors," pursuant to Regulation D, 17 C.F.R. § 230.501(a). Rule 501(a) promulgated pursuant to the 1933 Act.

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21. The PPM represented, *inter alia*, as follows: Phoenix sought investment of ten million dollars, at \$5.00 per share; by 2001 Phoenix had recovered from the effects of Hurricane Andrew; sales productivity was hampered by lack of working capital; with appropriate investment, Phoenix would experience "exponential growth;" and proceeds from the sale of \$10,000,000 of securities would be used for "new office and showroom setup, marketing investment, demo vehicles and platforms, production equipment and upgrades, debt repayment, and working capital."

22. Phoenix needed and sought immediate and substantial capital infusions. In 2001, Phoenix was in arrears and in default on approximately \$2.6 million in debt to First Union Bank. Defendant Shuler was a personal guarantor on the First Union debt. The First Union debt carried with it restrictive covenants which limited Phoenix's ability to, among other things, secure additional financing. As a further consequence, Phoenix's ability to obtain purchase orders and to manage and finance day-to-day proposals and orders for their products was limited.

23. The Phoenix Fiscal Year ends on March 31. In the Fiscal Year ending March 31, 2001, Phoenix reported less than \$1 million in gross revenue.

The Initial Contacts

24. In August 2001, Burman was approached by an investment advisor named George Schwelling ("Schwelling"). Schwelling told Burman of an opportunity to invest in Phoenix. Prior to his conversation with Schwelling, Burman had never heard of Phoenix. Plaintiff Warriner was first informed of Phoenix by Burman.

25. In May, 2002, Zawatsky was also told by Schwellings of an opportunity to invest in Phoenix. Prior to that conversation, Zawatsky had never heard of Phoenix.

26. Rolinski was contacted by Charles Levy in 2001. Levy and Rolinski were long time acquaintances and had worked together before on other investment deals and projects. In 2001, Levy advised Rolinski of the opportunity to invest in Phoenix. Prior to that discussion, Rolinski had never heard of Phoenix.

27. In May, 2002, Zawatsky, was contacted by Phoenix agent and representative Levy.

The Solicitation Period

28. From September 2001 through January 2003 (the "Solicitation Period"), the Phoenix Defendants, through Levy, solicited Plaintiffs to purchase Phoenix securities.

29. During the Solicitation Period, Levy engaged in over forty telephone conversations with Burman, over one hundred telephone conversations with Rolinski, and over sixty telephone conversations with Zawatsky. Those telephone conversations related to the purchase and the sale of Phoenix securities. Typically, Zawatsky spoke to Levy from Zawatsky's offices in the District of Columbia. Typically, Rolinski spoke to Levy from her offices in Maryland. Typically, Burman spoke to Levy from his office in Washington, D.C. Typically, when Zawatsky, Rolinski and Burman successfully placed calls to Levy, the calls would be made to North Carolina or Florida.

30. During the Solicitation Period, Levy advised Plaintiffs that each share would be sold for five dollars (\$5.00), except that, on August 27th, 2002, Shuler, in an investor update letter, advised shareholders that the price per share would rise to ten dollars (\$10.00) as of September 2, 2002. During the Solicitation Period, Levy represented that

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Phoenix intended to “go public” by January 2004, and he stated that shares would be sold in a public offering at between \$20 and \$100 per share.

31. Levy, on behalf of Phoenix, during the Solicitation Period, made the following statements, in addition to the Contract Misrepresentations and the IRS Misrepresentations, to Plaintiffs about Phoenix’ capabilities and activities: Phoenix had representatives who testified before Congress, sat on a “top secret” homeland security committee, and were actively setting policy within the U.S. government concerning security issues; Phoenix possessed a “secret” manufacturing plant across the Interstate from its main facility which was being used to produce “top secret” security items for the U.S. Government and other foreign governments; Phoenix was already in production of seven different types of sensors which had the capabilities to “hear”, “see” and “smell” in order to locate and identify targets and to focus laser beams on a target to enable Predator Drone Planes to destroy such targets; these sensors were already in use by the Department of Defense in Afghanistan and that one such target was Osama Bin Laden, who may have been cornered in a cave in Tora Bora; Phoenix’s profit margins were in excess of 35% on all government contracts; Phoenix’s immediate and near term share value would increase from \$5 a share to between \$20 and \$40 a share; Shuler is the key individual in Phoenix; Phoenix maintains a \$10,000,000 life insurance policy on Shuler for the benefit of Phoenix; no material decision regarding Phoenix was ever made without Shuler’s consent, knowledge or direction.

The Contract Misrepresentations

32. In Addendum E to the August 1, 2001 PPM, Phoenix claimed the following *risk adjusted* gross revenue for three years.

Year 1 -- \$388,313,910;

Year 2 -- \$599,655,509; and

Year 3 -- \$695,145,567, totaling \$2,885,087,858 for the three years. A true and

accurate copy of Addendum E is annexed to the Second Amended Complaint as *Exhibit 1* and is adopted and incorporated herein by reference as if specifically set forth herein.

33. Addendum E specifically and explicitly adjusted and analyzed Phoenix's scheduled gross income pursuant to a delineated risk assessment applied to a set of identified product sales ranging from a high of 100% to a low of 5%.

34. In Year 1: \$9,000,000 was risk adjusted at 100%; \$189,029,044 was risk adjusted at 80%; \$31,086,000 was risk adjusted at 90%; \$82,700,207 was risk adjusted at 10%; and, \$76,498,659 was risk adjusted at 5%.

35. In Year 2: \$13,000,000 was risk adjusted at 100%; \$212,657,675 was risk adjusted at 90%; \$14,250,000 was risk adjusted at 95%; \$206,750,517 was risk adjusted at 25%; and \$152,997,318 was risk adjusted at 10%.

36. In Year 3: \$17,000,000 was risk adjusted at 100%; \$372,150,930 was risk adjusted at 45%; and \$305,994,636 was risk adjusted at 20%.

37. A total of \$39,000,000 in gross revenue was, according to Phoenix's representations in Addendum E, a 100% certainty for Years 1 through 3; an additional total of \$14,500,000 was a 95% certainty in Year 2; an additional \$243,743,675 was a 90% certainty in Years 1 and 2; and, an additional \$189,029,044 was an 80% certainty in Year 1. *See Exhibit 1.*

38. On September 3, 2001, Phoenix prepared a written statement (the "September 2001 Contracts Statement") which purported to set out in color-coded format various

“Contracts in Progress.” A true and accurate color copy of the September 2001 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein. A black and white copy is annexed hereto as Exhibit 2 for convenience. The September 2001 Contracts Statement identified 21 contracts.

39. Of those contracts, 7 were highlighted in blue, 9 were highlighted in yellow, and 5 were highlighted in green. The legend on the September 2001 Contracts Statement provided as follows: Blue – “Signed Contracts;” Yellow – “Contracts in Process of being Signed;” Green – “Contracts Pending.”

The I&B and Rolinski Transactions

40. In February of 2002, Levy represented by telephone, to Rolinski in Maryland, that Phoenix had procured a contract (the “Border Contract”) with the then Immigration and Naturalization Service, now the U.S. Citizenship and Immigration Services of the Department of Homeland Security, to install sensors along the southern border of the United States. Levy further stated that “Phoenix was already providing thousands of sensors to the INS” (the “Border Contract Misrepresentation”). Relying on the Border Contract Misrepresentation, Rolinski purchased 2,000 shares of Phoenix stock, at \$5.00 per share, on February 20, 2002.

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41. The Border Contract Misrepresentation was material to Rolinski’s decision to invest in Phoenix, and the truth would have assumed actual significance in Rolinski’s decision to invest in Phoenix. Rolinski would not have invested in Phoenix but for the Border Contract Misrepresentation.

42. The Border Contract Misrepresentation was false when made. The allegation of falsity is based upon Shuler's written statement, on December 6, 2002, ten months after the making of the Border Contract Misrepresentation, that: "PWI is in final negotiations to supply our sensors to assist in the monitoring of the southern and northern borders of the United States."(emphasis added). This statement by Shuler contradicts Levy's representation that the border contract was "executed and Phoenix was providing thousands of sensors to the INS" as of February 2002. The allegation of falsity is also based on Phoenix's actual gross revenue in Fiscal Years 1, 2 and 3, *see* para. 52 below, as well as the absence by Phoenix counsel of any assertion of the Border Contract, *see* para. 53 below, as well as the failure of the Phoenix Defendants, or their counsel, to produce at any time to Rolinski or to any other Plaintiff documentary support for the existence of the Border Contract, or for the existence of the Border Contract in February 2002, or for receipt of proceeds for the sale of sensors by Phoenix to the INS or its successor agency.

43. On May 15, 2002, Phoenix prepared a written statement (the "May 2002 Contracts Statement") that purported to be an update of the September 2001 Contracts Statement. The May 2002 Contracts Statement was again color-coded in blue, yellow and green, and contained a legend identical to the legend in the September 2001 Contracts Statement. A true and accurate copy of the May 2002 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein.

44. The May 2002 Contracts Statement identified 33 contracts. Of those contracts, 12 were highlighted in blue, 16 were highlighted in yellow, and 5 were

highlighted in green. Blue highlighted contracts on the May 2002 Contracts Statement totaled \$31,075,521.

45. A copy of the May 2002 Contracts Statement was delivered to Rolinski by Levy by way of an instrumentality of interstate commerce in June 2002.

46. Zawatsky spoke by telephone with Levy in the middle of May 2002. Several days later, on or about May 20, 2002, Zawatsky received from Levy and from Phoenix, via an instrumentality of interstate commerce, at Zawatsky's office in Washington DC, the following documents, among others: the PPM, Addendum E, the September 2001 Contracts Statement, and the May 2002 Contracts Statement.

47. Within one week of receipt of those documents, Zawatsky, from his office in Washington, DC, spoke by telephone with Levy to obtain information about Phoenix and the documents. That conversation took place subsequent to May 15, 2002 and prior to May 28, 2002.

48. Levy told Zawatsky in that conversation, that the two Contracts Statements were "updates to the Addendum E financial projections," and that the blue line items on the color-coded sheets were reflective of the 100% risk adjusted revenue items in Addendum E.

49. In that conversation, Levy also told Zawatsky that the blue line items on the May 2002 Contract Statement are "done deals" with a 100% probability of performance. When probed further by Zawatsky in that conversation, Levy said that the blue line contracts are performing and generating revenue. Levy also represented in that conversation that the line items designated in yellow were drafted and out for signature. Levy said that as soon as a yellow contract was signed, Phoenix would begin to ship the

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product and get paid on the contract. Levy explained that the items designated in green were pending and under negotiation at the moment. Zawatsky asked Levy that, if all of the items in both yellow and green were ignored and one just concentrated on the items in blue, would that be the minimum amount of sales revenue Phoenix was assured to generate over the next three years. Levy replied: "absolutely." (along with the Contract Statements, and Addendum E, the "Blue Contract Misrepresentations"). The Blue Contract Misrepresentations were false.

50. In that conversation, Zawatsky asked about the exit strategy for the investment. Levy replied that Phoenix expected that Phoenix would go public by January of 2004, thereby giving investors a viable exit strategy (the "Public Sale Statements"). Levy added that, in the interim, investors would receive dividends approximately equal to their \$5.00 per share investment as a result of the cash flow generated by the blue line contracts. Levy stated that dividends would commence as early as December 2002 (the "Dividend Statements").

51. Based upon the Blue Contract Misrepresentations, as well as the Public Sale Statements and the Dividend Statements, Zawatsky, on behalf of I&B, purchased 25,000 shares of Phoenix common stock at \$5.00 per share on May 28, 2002. The Blue Contract Misrepresentations, as well as the Public Sale Statements and the Dividend Statements were material to I&B's decision to invest in Phoenix, and the truth would have assumed actual significance in I&B's decision to invest in Phoenix. Had Levy and Phoenix not made the Blue Contract Misrepresentations, I&B would not have invested in Phoenix.

52. The allegations of falsity of the Blue Contract Misrepresentations are based on the amounts of revenue reflected on each of Phoenix's audited financial statements.

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During this three year period, i.e., Fiscal Years ending March 31, 2002, March 31, 2003, and March 31, 2004, Phoenix actually received only approximately one three hundredth (1/300th) of the revenue set out in Addendum E to the PPM. Phoenix reported in audited financial statements actual revenue from all sources of: Fiscal Year 2002 -- \$929,606; and Fiscal Year 2003 -- \$2,965,064. The unaudited monthly cash flow statements for Fiscal Year 2004 reflect \$5,160,155 in sales revenue. The actual revenues of \$9,034,825, therefore, were more than 75% below the \$ 39,000,000 in revenues that Phoenix had stated in Addendum E that Phoenix was 100% certain to receive in this period.

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53. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, Phoenix has failed, when confronted with the possibility of this lawsuit, to produce any of the contracts claimed in the Blue Contract Misrepresentations. Further, in the Phoenix Defendants' own Motion to Dismiss the Complaint, they appear to assert only the existence of a "\$10 million dollar US Department of Defense contract for delivery of sensors." *Memorandum*, at 11, n.2. They make no claim of any kind of any other "blue" contract.

54. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, in the supplement to the Phoenix PPM appended to an August 12, 2002, investor update letter, Shuler wrote that Phoenix was "awaiting orders for proposed projects" from Venezuela. However, the May 2002 Contracts Statement identifies that item as a "blue" contract. In that same supplement, Phoenix wrote that it was "awaiting orders" for two Saudi Arabian contracts, notwithstanding that, in the May 2002 Contracts Statement, the Saudi Arabia items were identified as a "blue" contract and as a "yellow" contract.

55. In addition, as further evidence of the falsity of the Blue Contract Misrepresentations, at a meeting of the Phoenix Board of Directors, after the Plaintiffs had made the vast bulk of their investments in the Phoenix securities, Shuler attempted, for the first time, to explain the Blue Contract Misrepresentations. To the shock and surprise of Zawatsky, who as a result of Trust Communities Inc.'s \$2 million dollar loan to Phoenix had been added as a member of the Phoenix Board of Directors, Shuler indicated that the Phoenix "contracts" were not for a firm number of products or dollars, but were essentially options given to purchasers to order, at a purchaser's discretion, products covered by a contract.

56. In the second half of May 2002, Levy and Phoenix forwarded to Rolinski in Maryland by US mail the May 2002 Contracts Statement.

57. In or around June of 2002, Levy telephoned Rolinski in Maryland and told her that Phoenix had been awarded a \$10 million U.S. Department of Defense contract for the delivery of "sensors" (the "DOD Sensor Contract"). Rolinski queried Levy about the Contracts Statements. Levy made the Blue Contract Misrepresentations to Rolinski in that telephone conversation and urged Rolinski to invest further in Phoenix. Levy did not correct the Border Contract Misrepresentation. On the basis of the Blue Contract Misrepresentations, and continuing to rely on the Border Contract Misrepresentation, Rolinski, on June 24, 2002, purchased an additional 900 shares of Phoenix common stock at \$5.00 per share.

58. The Blue Contract Misrepresentations were material to Rolinski's decision to invest in Phoenix, and the truth would have assumed actual significance in Rolinski's decision to invest in Phoenix. Rolinski would not have invested for the second time in

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Phoenix but for the Blue Contract Misrepresentations, and but for the Border Contract Misrepresentation and the failure to correct the Border Contract Misrepresentation.

59. On or around July 1, 2002, Levy telephoned Zawatsky in his office in Washington, D.C. and told Zawatsky that Levy had "great news." Levy advised Zawatsky that Phoenix had secured the DOD Sensor Contract, and Levy urged Zawatsky to invest further in Phoenix on behalf of I&B. Levy did not correct the Blue Contract Misrepresentations. Zawatsky asked Levy when revenue would be generated from the DOD Sensor Contract. Levy stated that sensors would begin to be shipped immediately. Levy also stated that the cash flow generated by the sensor sales pursuant to the \$10,000,000 contract would allow Phoenix to pay the investors a dividend of nearly all of the \$5.00 per share price by December of 2002. As is more fully set forth in paragraph 60 below, the Phoenix Board of Directors subsequently passed a resolution setting out the Phoenix policy on declaration of dividends.

As a result of Levy's statements, as set forth in the preceding paragraph, and the impact of that purported contract on Phoenix's immediate cash flow and its ability to pay dividends as promised, and as a result of the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, I&B, on July 8, 2002, purchased an additional 25,000 shares of Phoenix common stock at \$5.00 per share.

60. On July 16, 2002, Zawatsky and two advisers traveled to Florida to inspect the Phoenix facility and to meet with Shuler. During his inspection, Zawatsky specifically inquired of Shuler if Phoenix had the ability to meet the immediate, imminent, urgent and substantial production demands of the DOD Sensor Contract. Shuler made no attempt to advise Zawatsky that the DOD Sensor Contract production

requirements were not imminent, or did not require immediate and substantial production. Instead, Shuler showed Zawatsky the manufacturing facility and stated that hundreds of sensors could be completed and shipped per week by using three production shifts. Shuler represented to Zawatsky that Phoenix was capable of meeting immediately all of the production requirements of the DOD Sensor Contract. Neither Shuler nor anyone at Phoenix corrected the Blue Contract Misrepresentations, or indicated that the DOD Sensor Contract was not for immediate production and sales, or that it gave the Department of Defense the right to order only a few sensors and was not a binding obligation of the Department of Defense to take and pay for \$10,000,000 of sensors in the short term (the "DOD Sensor Omission").

On July 21, 2002, Shuler and the Phoenix Board of Directors passed a resolution adopting a "liberal and aggressive dividend policy...", designing a procedure to "aggressively pursue" by the end of 2002 a plan to go public, and providing specifically that: "...(c) ... upon the culmination of the current Fiscal Year, the Board herein agrees to declare and pay a dividend to all shareholders of record up to a maximum of five dollars (\$5.00) per share...."

61. As a result of the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and as a further result of the July telephone conversation with Levy, see para. 59 above, and the statements of Shuler to Zawatsky in Florida, see para. 60 above, I&B, on July 22, 2002 purchased an additional 100,000 shares at \$5.00 per share.

62. The Blue Contract Misrepresentations, the failure to correct the Blue Contract Misrepresentations, and the statements made by Shuler to Zawatsky in Florida were

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material to I&B's decision to invest in Phoenix, and the truth would have assumed actual significance in I&B's decision to invest for the second and third time in Phoenix . I&B would not have invested a second and third time, increasing I&B's investment in Phoenix by a factor of 6 - from \$125,000 to \$750,000- if Levy and the Phoenix Defendants had not made the Blue Contract Misrepresentations, or if Levy or the Phoenix Defendants had corrected the Blue Contract Misrepresentations or had not made the DOD Sensor Omission.

63. On August 2, 2002, Phoenix prepared a written statement (the "August 2002 Contracts Statement") that purported to be an update of the September 2001 Contracts Statement and the May 2002 Contracts Statement . The August 2002 Contracts Statement was again color-coded in blue, yellow and green, and contained a legend identical to the legend in the September 2001 Contracts Statement and the May 2002 Contracts Statement. A true and accurate copy of the August 2002 Contracts Statement is annexed to the Complaint as *Exhibit 2*, and is adopted and incorporated herein by reference as if specifically set forth herein, and the representations contained therein comprise in part the Blue Contract Misrepresentations. The August 2002 Contracts Statement identified 35 contracts. Of those contracts, 15 were highlighted in blue, 15 were highlighted in yellow, and 5 were highlighted in green. Blue highlighted contracts on the August 2002 Contracts Statement totaled \$1,981,075,523.

64. The August 2002 Contract Statements were delivered by Shuler through the means and instrumentalities of interstate commerce to I&B, Rolinski and Burman on or about August 12, 2002.

65. As is set forth in Paragraphs 52 through 55 above, the August 2002 Contracts Statement was false.

66. In or around January of 2003, Levy again telephoned Rolinski in Maryland and told her that Phoenix had procured a billion dollar contract with Egypt . Levy represented in that conversation with Rolinski that Shuler had gone to Egypt personally and procured the contract (the "Egypt Contract Misrepresentation"). In that telephone conversation, Rolinski and Levy discussed the Addendum E risk adjusted revenues. Levy told Rolinski that "investing in Phoenix carries a non-existent risk factor," (the "Risk Factor Statement") based on Addendum E. Levy did not correct the Border Contract Misrepresentation, or the Blue Contract Misrepresentations. Based on the Border Contract Misrepresentation, and the failure to correct the Border Contract Misrepresentation, and the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and the Egypt Contract Misrepresentation, and the Risk Factor Statement, Rolinski, on January 15, 2003, purchased 2000 shares of Phoenix common stock at \$10.00 per share, more than doubling her previous investment.

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67. The Border Contract Misrepresentation, and the failure to correct the Border Contract Misrepresentation, and the Blue Contract Misrepresentations, and the failure to correct the Blue Contract Misrepresentations, and the Egypt Contract Misrepresentation and the Risk Factor Statement were material to Rolinski's decision to invest in Phoenix for the third time, and the truth would have assumed actual significance in Rolinski's decision to invest in Phoenix for the third time, more than doubling her extant investment in Phoenix securities. Had Levy not made the Border Contract Misrepresentation, and failed to correct the Border Contract Misrepresentation, and had Levy and the Phoenix

Defendants not made the Blue Contract Misrepresentations, and failed to correct the Blue Contract Misrepresentations, and had Levy not made the Egypt Contract Misrepresentation and the Risk Factor Statement, Rolinski would not have invested in Phoenix for the third time.

68. These misrepresentations were false when made. The allegations of falsity are set out in Paragraphs 52 through 55 above.

69. In addition, as further evidence of the falsity of the Egypt Contract Misrepresentation, the allegations of falsity are based upon Shuler's statements in the March 4, 2003, investor update letter which reads in pertinent part, "In December 2002, I traveled to Egypt with the expressed purpose of signing the first delivery order for our approximate \$600 million National Intelligence Support System (NISS). *We have submitted all of the required information to the Ministry of Interior and are waiting as the project moves through their bureaucracy in order for it to receive all of the required approvals.*" Emphasis in original. Phoenix's own documents confirm that no contract was signed in January of 2003 with Egypt and in fact that the proposal was not for a billion dollar contract, but, at best, a \$600 million dollar proposal.

The Warriner Transaction

70. Plaintiff Warriner had multiple telephone conversations with Levy. Warriner was in his office in Washington DC for those telephone conversations.

71. In August 2002, in a telephone conversation with Levy while Warriner was in the District of Columbia, Levy made to Warriner the Egypt Contract Misrepresentation.

72. On August 27, 2002, on the basis of the statements made by Levy and the Egypt Contract Misrepresentation, Warriner purchased 5000 shares of Phoenix common stock at \$5.00 per share.

73. The Egypt Contract Misrepresentation was material to Warriner's decision to invest in Phoenix and the truth would have assumed actual significance in Warriner's decision to invest in Phoenix. Had Levy not made the Egypt Contract Misrepresentation, Warriner would not have invested in Phoenix.

The Burman Transactions

74. In the summer of 2001, Plaintiff Burman, at age 83, traveled to Florida to inspect the Phoenix facilities, and to meet with Shuler and Levy. Levy and Shuler advised Burman that Phoenix had a "secret facility" and that most of Phoenix's products and contracts were "classified" and could not be seen without top security clearances. During that visit, Levy represented to Burman that Phoenix had negotiated the DOD Sensor Contract.

75. In September 2001, prior to the purchase by Burman of Phoenix securities, Levy and the Phoenix Defendants delivered to Burman the September 2001 Contracts Statements, see para. 39 above.

76. Burman purchased 61,400 shares of common stock in Phoenix at \$5.00 for \$307,000 in 12 successive transfers, as follows: September 25, 2001, in the amount of \$20,000; on September 25, 2001, in the amount of \$2000; on November 3, 2001, in the amount of \$25,000; on December 19, 2001, in the amount of \$50,000; on March 1, 2002, in the amount of \$30,000; on May 20, 2002, in the amount of \$20,000; on August 2, 2002, in the amount of \$50,000; on August 28, 2002, in the amount of \$50,000; on

August 30, 2002, in the amount of 10,000; on September 1, 2002, in the amount of \$25,000; on September 1, 2002, in the amount of \$12,500; and, on September 1, 2002, in the amount of \$12,500.

77. In August of 2002, Burman was provided with the August 2002 Contracts Statement.

78. Prior to September 2002, Levy made to Burman in his office in Washington, D.C., by telephone, the Egypt Contract Misrepresentation. Levy never corrected the statements made in the September 2001 or August 2002 Contracts Statements, and never corrected the Egypt Contract Misrepresentation.

79. The Egypt Contract Misrepresentation, the September 2001 and August 2002 Contracts Statements were material as of the date that they were made to Burman's decisions to invest in Phoenix, and the truth would have assumed actual significance in Burman's decision to invest in Phoenix.

80. After making his investment in Phoenix on September 1, 2002, Burman asked Levy when Phoenix would receive payment under the DOD Sensor Contract. Levy finally informed Burman that the DOD Sensor Contract was not a binding obligation, but merely gave DOD the right to acquire at its discretion, up to \$10 Million in sensors from Phoenix.

81. The Contract Misrepresentations were false when made, and were known by Levy and by the Phoenix Defendants to have been false when made. The Phoenix Defendants acted with scienter in that they knew that the statements made by Levy and Shuler were materially false and misleading. They also knew that the documents issued and/or disseminated in the name of Phoenix were materially false and misleading.

Phoenix and Shuler also knew that such statements or documents would be issued or disseminated to the Plaintiffs and were in fact issued and disseminated to the Plaintiffs. They also knew and intended that the Plaintiffs would rely on such misstatements and documents, and they knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements and documents. The Contract Misrepresentations are: the Border Contract Misrepresentation; the Blue Contract Misrepresentations; the Egypt Contract Misrepresentation. The Blue Contract Misrepresentations include the oral statements as set forth above, Addendum E, and the Contracts Statements.

82. Shuler had a motive to make the Contract Misrepresentations.
83. Shuler had the opportunity to make the Contract Misrepresentations.
84. Phoenix had a motive to make the Contract misrepresentations.
85. Phoenix had the opportunity to make the Contract Misrepresentations.
86. In reasonable reliance on the misrepresentations and omissions of the Phoenix Defendants, Plaintiffs transferred to Phoenix a total of \$1,116,500 in exchange for a total of 223,300 shares of Phoenix securities.

The IRS Misrepresentations

87. In connection with the sale of Phoenix's securities, the Plaintiffs were provided with the Company's audited financial statements prepared by R&C.
88. The financial statements dated March 31, 2002-2001, contain notes to the financial statements. Specifically, Note 10, titled "Commitments and Contingencies" contains an averment regarding payroll taxes. Note 10 reads in pertinent part, "Included in accounts payable and accrued expenses at year end are accrued payroll taxes. The

payroll taxes were past due and the Company may be subject to penalties and Interest.

No penalties or interest has been imposed. In August 2002 past due payroll taxes were paid (see Note 13)". Note 13, titled "Subsequent Events", makes further representations regarding the unpaid employment taxes. Note 13 reads in pertinent part, "The Company's payroll taxes were past due at year end (see Note 10). In August 2002, the Company paid all current and overdue payroll taxes."

89. In May 2002, after reviewing the March 31, 2001-2000 audited financial statements, which indicated in Note 9 unpaid employment taxes, Zawatsky questioned Levy about such unpaid employment taxes. Zawatsky was told by Levy that the unpaid employment taxes had in fact been paid in 2002, after March 31. That statement by Levy was false.

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90. During his visit to Phoenix on July 16, 2002, Zawatsky asked Shuler directly about the unpaid employment taxes. Shuler told Zawatsky that the unpaid employment taxes had been paid and that the March 31, 2002-2001 audited financial statements would reflect that payment (along with the financial statements, the "IRS Misrepresentations"). As set forth in para. 88, the March 31, 2002-2001 audited financial statements prepared by R&C as of June 12, 2002, and September 26, 2002, did represent in Notes 10 and 13 that the unpaid employment taxes had been paid in August, 2002. Shuler's statement that the unpaid employment taxes had been paid was false.

91. As evidence of the falsity of the IRS Misrepresentations, on or around, April 13, 2004, a letter was sent to Robert Pugh, CPA, the CFO of Trust Communities, Inc., from the IRS stating that Phoenix was liable for unpaid employment taxes (Forms 940 and 941) from the 1998-2003 tax years and that the IRS had placed a tax lien against

Phoenix's real property. The letter stated, "The amount needed to fully pay all liabilities and release the lien is \$233,677.95." A true and correct copy of the April 13, 2004 letter is attached hereto as Exhibit 3 and it is adopted and incorporated herein as is specifically set forth herein.

92. The Phoenix Defendants and R&C issued materially false and misleading financial statements and omitted to disclose material information regarding the status of Phoenix's unpaid employment taxes (Forms 940 and 941) from the 1998-2003 tax years.

93. The Phoenix Defendants knew and should have known that they owed to the IRS at the time that they made the IRS Misrepresentations unpaid employment taxes and should have disclosed this fact to the Plaintiffs prior to their investments.

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94. When Phoenix's financial statements were audited by R&C for the referenced time periods, R&C should have disclosed the unpaid taxes in its audit reports. R&C audit reports for 1999-2003 were provided to the Plaintiffs by the Phoenix Defendants and R&C, but the 2002-2001 and 2003-2002 audited financial statements failed to disclose the unpaid employment taxes. Indeed, the 2002-2001 audited statements reported that the taxes had been paid. According to R&C, Phoenix was responsible for making its tax payroll payments and "many of them had been made late" for the period of 1999 to 2004". See Declaration of Carl N. Howden, December 24, 2004, appended to Rachlin Reply Memorandum In Support of Suggestion of Responses of Motion to Dismiss, filed December 23, 2004.

According to R&C, Phoenix paid over \$16,000 in payroll tax liabilities no earlier than November 15, 2004, but arising out of claimed deficiencies from 1999-2004.

95. The Phoenix Defendants and R&C failed to disclose to Plaintiffs the unpaid taxes. Zawatsky called R&C immediately after Zawatsky learned of the IRS tax lien and the unpaid employment taxes. Zawatsky was told that R&C would have Carl Howden ("Howden") "get right on" the unpaid tax issue. Zawatsky later spoke with Howden who acknowledged that he had not resolved the issue. Plaintiffs, prior to the initiation of this litigation, were never supplied with any additional information concerning the unpaid employment taxes, and the Phoenix Defendants, failed to correct the IRS Misrepresentations prior to the initiation of this litigation.

96. The failure to disclose the unpaid taxes was material to each Plaintiff's decision to invest in Phoenix, and the truth would have accrued actual significance in their decisions to invest in Phoenix. Had the Phoenix Defendants or R&C disclosed the unpaid employment taxes, no Plaintiff would have invested in Phoenix.

Count 1

(Violation of Section 10(b) Of the Exchange Act And Rule 10b-5 Promulgated Thereunder By Defendants Phoenix and Shuler)

97. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 96 of the Second Amended Complaint as if fully set forth herein.

98. The Phoenix Defendants carried out a plan, scheme and course of conduct which was intended to and did deceive the Plaintiffs as alleged herein and cause the Plaintiffs to purchase Phoenix securities. In furtherance of this unlawful scheme, plan and course of conduct, the Phoenix Defendants took the actions set forth herein.

99. The Phoenix Defendants employed devices, schemes, and artifices to defraud, directly and indirectly, caused false statements to be made to the Plaintiffs as specified

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herein and failed to state material facts to the Plaintiffs as set forth herein, and engaged in acts, practices, and a course of business which operated as a fraud and deceit upon the Plaintiffs in violation of Section 10(b) of the Exchange Act and Rule 10b-5.

100. The Phoenix Defendants, directly and indirectly, by the use, means or instrumentalities of interstate commerce, including use of the telephones, mails, wires and the Internet, disseminated the materially false statements and omissions referenced herein. The initial definitions of such statements and omissions are set out in paragraphs 16, 17, 40, 49, 66 and 81.

101. The Phoenix Defendants knew and should have known that the Contract Misrepresentations and the IRS Misrepresentations (collectively, "the Misrepresentations") specified above were untrue when made and that the truth and the omissions would have been material to the Plaintiffs' decision to participate in the offering of Phoenix securities. The Phoenix Defendants made the Misrepresentations, and omitted the omissions, knowingly and willfully, and with such extreme recklessness that the misconduct rose to the level of fraud.

Defendant Shuler had an improper motive to mislead Plaintiffs, including the desire to minimize his personal liability, and to minimize the risk to his personal investment in Phoenix, and to maximize his personal profit from Phoenix, at the risk and at the expense of Plaintiffs. Defendant Shuler had multiple opportunities to mislead Plaintiffs, including his exercise of complete control over Phoenix, and its agents.

Defendant Phoenix had an improper motive to mislead Plaintiffs, including the improper desire of Phoenix to advance and to protect the personal interests of Shuler, and to induce Plaintiffs to invest monies in Phoenix without meaningful disclosure of

Phoenix's financial position, and then-existing contractual commitments. Defendant Phoenix had multiple opportunities to mislead Plaintiffs by its direct and complete control, through its officers and agents, of information material to the decisions of the Plaintiffs to purchase Phoenix securities.

The Misrepresentations were made by the Phoenix Defendants, using fraudulent means, and material facts were concealed from the Plaintiffs with the specific intent to cause the Plaintiffs to transfer funds to Phoenix in exchange for Phoenix securities.

102. At the time of the described Misrepresentations, Plaintiffs were ignorant of their falsity and believed them to be true and had no knowledge of the existence of the material factual omissions.

103. Plaintiffs reasonably relied upon the Misrepresentations of the Phoenix Defendants and, as a consequence, transferred \$1,116,500, in the specific sums and on the specific dates set out herein, to Phoenix in exchange for Phoenix securities.

104. The conduct of the Phoenix Defendants, described above, constitutes a violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.

105. As a direct and proximate result of the wrongful conduct of the Phoenix Defendants, Plaintiffs suffered damages in connection with their purchases, as set forth herein, of Phoenix securities, in an amount equal to the purchase price of the securities.

Count Two
(Common Law Fraud, Deceit and Misrepresentation
By Defendants Phoenix and Shuler)

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106. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 105 of the Second Amended Complaint as if fully set forth herein.

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107. To induce the Investors to transfer \$1,116,500 to Phoenix in exchange for Phoenix Securities, the Phoenix Defendants made to Plaintiffs, at the times and in the places set forth herein, the Contract Misrepresentations and the IRS Misrepresentations, and continuously thereafter failed and refused to correct the Misrepresentations. The initial definitions of such Misrepresentations are set out in paragraphs 16, 17, 40, 49, 66 and 81.

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108. When the Phoenix Defendants made these Misrepresentations to Plaintiffs, the Phoenix Defendants knew they were false and misleading, and the Misrepresentations were made with the intent to deceive Plaintiffs and induce Plaintiffs to purchase Phoenix securities, and the Misrepresentations were made with such extreme recklessness and disregard for the truth as to rise to the level of fraud.. The Phoenix Defendants also knew that by failing to state facts material to Plaintiffs' decisions to participate in the offering, and by failing to correct the Misrepresentations, the Phoenix Defendants were misleading Plaintiffs, and the Phoenix Defendants did so with the intent to deceive Plaintiffs and induce Plaintiffs to purchase Phoenix securities.

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109. Plaintiffs reasonably relied on the Misrepresentations and failures to state material facts, and failures to correct the Misrepresentations, and in reliance thereon, Plaintiffs transferred \$1,116,500 to Phoenix for the purchase of securities in the sums and on the dates set forth herein.

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110. But for the Misrepresentations and failures to state material facts, and failures to correct the Misrepresentations, by the Phoenix Defendants, Plaintiffs would not have purchased any Phoenix securities, and Plaintiffs relied to their detriment on the Misrepresentations and failures to state material facts, and failures to correct the

Misrepresentations. The Phoenix securities purchased by Plaintiffs are worth, if anything, substantially less than the price paid by Plaintiffs to purchase the securities.

111. The acts and omissions of the Phoenix Defendants, as set forth above, directly and proximately caused damages to Plaintiffs, and as a result, the Plaintiffs lost \$1,116,500, collectively, plus interest thereon, since the dates of Plaintiffs' investments, in the amounts and on the dates set forth herein.

112. The willful and intentional fraud of Defendants Phoenix and Shuler is accompanied by such a high degree of scienter as to render the Phoenix Defendants liable for punitive damages in an amount to be proven at trial, but in any event not less than \$100,000.00 for each plaintiff.

Count Three

(Negligent Misrepresentation By Defendants Phoenix and Shuler)

113. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 112 of the Second Amended Complaint as if fully set forth herein.

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114. To induce the Investors to transfer \$1,116,500 to Phoenix in exchange for Phoenix securities, the Phoenix Defendants made to Plaintiffs at the times and in the places set forth herein, the Contract Misrepresentations and the IRS Misrepresentations, and failed to state material facts to Plaintiffs, and continuously thereafter failed and refused to correct the Misrepresentations, and made the Public Sale Statements, the

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Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission (the "Status Statements"). The initial definitions of such Misrepresentations and Statements are set out in paragraphs 16, 17, 40, 49, 50, 60, 66, 81 and 114.

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115. No dividends have been declared, paid or issued by Phoenix to Plaintiffs.

116. No public sale has been undertaken, nor the planning for any public sale concluded.

117. The risks associated with the purchase of the securities were and are well in excess of zero.

118. The DOD Sensor Contract was not, in 2002, for immediate production and sale, and did not, according to the subsequent and belated statements of the Phoenix Defendants, bind DOD to purchase sensors in any specific volume or dollar amount.

119. When the Phoenix Defendants made these Misrepresentations and failed to state material facts to Plaintiffs, and failed to correct the Misrepresentations, and made the Status Statements, they knew or should have known they were false and misleading and that Plaintiffs would rely thereon in order to decide whether to purchase Phoenix securities.

120. Plaintiffs did in fact rely on the Misrepresentations and the failures to state material facts, and the failure to correct the Misrepresentations, and the Status Statements as set forth herein, and such reliance was objectively reasonable. Reliance on the Misrepresentations and the failures to state material facts and the failure to correct the Misrepresentations, and the Status Statements was material to the investment decisions made by the Plaintiffs.

121. The acts and omissions of the Phoenix Defendants, as set forth herein, directly and proximately caused damages to Plaintiffs, and as a result, the Plaintiffs lost \$1,116,500, collectively, plus interest thereon, since the dates of Plaintiffs' investments, in the amounts and on the dates set forth herein.

Count Four**(Breach of Fiduciary Duties By Defendants Phoenix and Shuler)**

122. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1

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through 117 of the Second Amended Complaint as if fully set forth herein.

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123. The Phoenix Defendants owed to Plaintiff Burman fiduciary duties of

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loyalty, diligence and fairness commencing September 25, 2001.

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124. The Phoenix Defendants owed to Plaintiff Rolinski fiduciary duties of

loyalty, diligence and fairness commencing February 20, 2002.

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125. The Phoenix Defendants owed to Plaintiff I&B fiduciary duties of loyalty,

diligence, disclosure and fairness commencing May 28, 2002.

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126. The Phoenix Defendants owed to Plaintiff Warriner fiduciary duties of

loyalty, diligence, good faith and fairness commencing August 27, 2002.

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127. The Phoenix Defendants breached their fiduciary duties by making the

Contract Misrepresentations.

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128. The Phoenix Defendants breached their fiduciary duties by failing to correct

the Contract Misrepresentations.

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129. The Phoenix Defendants breached their fiduciary duties by making the IRS

Misrepresentations.

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130. The Phoenix Defendants breached their fiduciary duties by failing to correct

the IRS Misrepresentations.

131. The Phoenix Defendants breached their fiduciary duties by making the Public Sale Statements, the Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission.

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132. The Phoenix Defendants breached their fiduciary duties by failing to correct the Public Sale Statements, the Dividend Statements, the Risk Factor Statement and the DOD Sensor Omission.

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133. The initial definitions of such Misrepresentations and Statements are set out in paragraphs 16, 17, 40, 49, 50, 60, 66, 81 and 114.

Deleted: 129. The Phoenix Defendants breached their fiduciary duties by failing to secure for Phoenix the income from those Contracts identified on Addendum E as having 100% certainty.¶

134. As a direct, proximate and foreseeable consequence of these breaches of fiduciary duty, Plaintiffs Burman, Rolinski and I&B were wrongly induced to purchase additional shares of Phoenix stock which are now worthless of nearly worthless.

130. The Phoenix Defendants breached their fiduciary duties by failing to secure for Phoenix the income from the Contracts, identified in blue, on the May 2002 and the August 2002 Contracts Statements, and on the Contracts statements issued thereafter.¶

131. The Phoenix Defendants breached their fiduciary duties by failing to secure for Phoenix the income from the Contracts, identified in yellow, on the May 2002 and the August 2002 Contracts Statements, and on the Contracts statements issued thereafter.¶

132. The Phoenix Defendants breached their fiduciary duties by failing to conclude negotiations for, and secure for Phoenix the income from the Contracts, identified in green, on the May 2002 and the August 2002 Contracts Statements, and on the Contracts Statements issued thereafter.¶

133.

Count Five **(Violation of State Blue Sky Laws By Defendants Phoenix and Shuler)**

135. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 133 of the Second Amended Complaint as if fully set forth herein, and restate with particularity the averments of Count One herein as if they are repeated verbatim in this Count..

Deleted: , and all Plaintiffs sustained loss and damage in an amount equal to their *pro rata* interest in the income that Phoenix failed to secure from the contracts identified on Addendum E as 100% certain and on the Contracts Statements identified in blue

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136. The Misrepresentations made by the Phoenix Defendants, and the failure to state material facts, and failure to correct the Misrepresentations, were in violation of the blue sky state security statutes of the District of Columbia, D.C. Code § 3-3602 (2001), 31-5605.02 (2001, Replacement Vol. 2005) and the State of Maryland. Section 11-301 of the Maryland Securities Act. The initial definitions of such Misrepresentations are set out in paragraphs 16, 17, 40, 49, 66 and 81.

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137. Plaintiffs sustained injury and damage as a consequence of the violations by the Phoenix Defendants of the blue sky state securities statutes of the District of Columbia and the State of Maryland, including the loss of monies paid to Phoenix, in the amounts and on the dates set forth herein, for the purchase of Phoenix securities.

Count Six **(Appointment of a Receiver for Phoenix)**

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138. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 136 of the Second Amended Complaint as if fully set forth herein.

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139. Phoenix has failed and refused, despite repeated demands, to convene a shareholders' meeting. A shareholders' meeting is a requirement of state law, including Florida law. Following repeated demands a shareholders' meeting was scheduled for September 28, 2005. Phoenix cancelled the shareholders' meeting on September 15, 2005.

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- a) examine and correct the public statements of

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- b) examine and secure, to the extent possible, the contracts, and income from the contracts identified by Phoenix on Addendum E and the Contracts statements;¶
- c) examine, terminate

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- d) prepare, complete and disseminate to Plaintiffs and to the court a comprehensive

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Deleted: e) pay all outstanding taxes; and¶

- f) take such other actions as are necessary and appropriate to the protection of the non-insider shareholders of Phoenix.¶

¶

Count Seven

(Injunctive Relief Against the Phoenix Defendants)

139. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 138 of the First Amended Complaint as if fully set forth herein.¶

142. Though purporting to reflect a period ending March 31, 2004, the FY 2004 Statement included a January 26, 2005 event, as well as several other events – related to payroll taxes - which took place after March 31, 2004.

143. Plaintiffs have received from Phoenix no financial information subsequent to receipt of the FY 2004 Statement.

144. The FY 2004 Statement showed:

a. Cash and accounts receivable of \$313,079;

b. Accounts payable and accrued liabilities of \$671,544;

c. Current assets which were incorrectly inflated by out-of-date or non-

current inventory;

d. Receipt by Shuler from Phoenix, during the reported year, of

\$352,000. That sum represented a salary increase of 33%, or \$48,000.

During the same period, accounts payable and accrued liabilities increased

by \$571,986, from \$159,588 to \$671,544.

e. Monthly selling, general and administrative expenses averaging

\$113,660, or over one-third of all available cash and receivables.

145. Phoenix out of date on non-current inventory is valueless – or virtually valueless – because Phoenix builds to contract, and has not regularly sold out of “inventory”.

146. The debt described in the Second Amended Complaint, at para. 4, was replaced in or about January 2005 by new debt, and included an additional debt of \$400,000. Taking into account the origination fee, the new debt has an effective interest

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rate of 15%. While the previous debt was secured by real estate, the new debt is secured by all Phoenix assets, and it is due in full February 1, 2006.

147. Phoenix is insolvent.

148. Phoenix is at great risk of further financial loss.

149. It is in the interest of Plaintiffs, and in the interest of all non-insider investors in Phoenix, and in the general public interest, that the court appoint a Receiver for Phoenix, who will:

- a) examine and correct the public statements of Phoenix;
- b) examine and secure, to the extent possible, the contracts, and income from the contracts identified by Phoenix on Addendum E and the Contracts statements;
- c) examine, terminate or suspend, and report to the court on the payments, if any, by Phoenix to Shuler, or to R&C, or to Levy;
- d) prepare, complete and disseminate to Plaintiffs and to the court a comprehensive financial statement for Fiscal Years 2001 through 2005;
- e) pay all outstanding taxes; and
- f) take such other actions as are necessary and appropriate to the protection of the non-insider shareholders of Phoenix.

Count Seven
(Injunctive Relief Against the Phoenix Defendants)

150. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 138 of the Second Amended Complaint as if fully set forth herein.

151. The balance of equities weighs in favor of full disclosure of the financial condition of Phoenix.

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152. The public interest weighs in favor of full disclosure of the financial condition of Phoenix.

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153. Plaintiffs are entitled as a matter of equity to a preliminary and a permanent injunction, decree and order directing the Phoenix Defendants to:

- a) correct the public statements of Phoenix;
- b) terminate or suspend, and report to the court on the payments, if any, by Phoenix to Shuler, or to R&C, or to Levy; and
- c) prepare, complete and disseminate to Plaintiffs and to the court a comprehensive audited financial statement for Fiscal Years 2001 through 2005.

Count Eight

(Negligence Against Defendant R&C)

154. Plaintiffs repeat and reallege the allegations set forth in paragraphs 1 through 142 of the Second Amended Complaint as if fully set forth herein.

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155. R&C owed a duty to Plaintiffs to act with the requisite degree of skill and care that reasonably competent public accountants follow when auditing the financial statements of a company for presentation to potential investors.

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156. When R&C audited the financial statements of Phoenix, they reasonably should have discovered that Phoenix had unpaid employment taxes (Forms 940 and 941) for the 1998 through 2003 tax years.

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157. Because R&C either did not discover the unpaid employment taxes of Phoenix and/or did not adequately report such information in the audited financial statements, R&C breached its duty to Plaintiffs by falling below the standard of care applicable to accountants in the same or similar situation.

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158. By not following that standard of skill and care, R&C's conduct was the direct and proximate cause of injury to the Plaintiffs. Plaintiffs would not have invested in Phoenix securities had R&C's audit reports disclosed the existence of unpaid employment taxes.

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159. As a direct and proximate result of the negligence of R&C, Plaintiffs suffered damages in the amount of \$1,116,500, collectively, plus interest in the amount of 10% per annum, since the respective dates of Plaintiffs' investments.

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WHEREFORE, Plaintiffs pray for relief and judgment as follows:

- a) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Burman against all Defendants, jointly and severally, in the amount of \$307,000.00, or such other amount as may be proven at trial;
- b) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Warriner against all Defendants, jointly and severally, in the amount of \$25,000.00, or such other amount as may be proven at trial;
- c) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff I&B against all Defendants, jointly and severally, in the amount of \$750,000.00, or such other amount as may be proven at trial;

- d) As to Counts One, Two, Three, Four and Five, an award of compensatory damages in favor of Plaintiff Rolinski against all Defendants, jointly and severally, in the amount of \$34,400.00, or such other amount as may be proven at trial;
- e) As to Counts Two and Four, an award of punitive damages, in an amount to be proven at trial, in favor of all Plaintiffs and against Defendant Phoenix.
- f) As to Counts Two and Four, an award of punitive damages, in an amount to be proven at trial, in favor of all Plaintiffs and against Defendant Shuler.
- g) As to Count One, an award of statutory damages;
- h) As to Count Five, an award of statutory damages;
- i) As to Counts One, Two, Four and Five, an award in favor of Plaintiffs and against the Phoenix Defendants, jointly and severally, of the reasonable attorneys fees incurred by Plaintiffs in the prosecution of this action;
- j) As to Count Six, the appointment of a receiver to take the actions set forth in Count Six;
- k) As to Count Seven, the entry of an injunction, decree, order or judgment directing the Phoenix Defendants to take the actions set forth in Count Seven;
- l) As to Count Eight, compensatory damages in favor of plaintiffs, in the amounts set forth in (a), (b), (c), and (d), above, against Defendant R&C;
- m) An award to Plaintiffs of costs;
- n) An award to Plaintiffs of prejudgment interest and post judgment interest; and
- o) Such other and further relief as the Court may deem just and proper.

Jury Demand

Plaintiffs demand a trial by jury of all issues so triable in this action.

Respectfully Submitted,

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