NIGHTHAWK SYSTEMS INC
Form 10QSB
May 16, 2007

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _________ to ________

Commission File Number: 0-30786

NIGHTHAWK SYSTEMS, INC.
(Exact name of small business issuer as specified in its charter)

Nevada	**87-0627349**
(State or other jurisdiction of incorporation or organization)	(I.R.S Employer Identification No.)

10715 Gulfdale, Suite 200

San Antonio, TX 78216

(Address of principal executive offices)

210 341-4811

(Issuer's telephone number)

(Former name, former address and former fiscal year, if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes [ ] No [ ]

APPLICABLE ONLY TO CORPORATE ISSUERS

As of May 15, 2007, there were 100,206,505 shares of common stock, par value $.001 per share, of the registrant issued and outstanding.

Transitional Small Business Disclosure Format (Check one): Yes [ ] No [X]

NIGHTHAWK SYSTEMS, INC.

INDEX

NIGHTHAWK SYSTEMS, INC.

CONDENSED CONSOLIDATED BALANCE SHEET

AS OF MARCH 31, 2007

(unaudited)

ASSETS	MARCH 31, 2007
Current assets:	
Cash	$88,544
Accounts receivable	83,720
Inventories	112,069
Prepaid expenses	28,865
Total current assets	313,198
Furniture, fixtures and equipment, net	16,419
Intangible assets	20,270
Other	217,705
	$567,592
LIABILITIES AND STOCKHOLDERS' DEFICIT	
Current liabilities:	
Accounts payable	$207,332
Accrued expenses	611,017
Line of credit	19,692
Notes payable:	
Convertible debt, net of discount of $882,129	1,858,925
Related parties	10,434
Other	184,640
Total liabilities (all current)	2,892,040
Commitments and contingencies	
Stockholders' deficit:	
Preferred stock, $0.001 par value; 5,000,000 shares authorized;	-
no shares issued and outstanding	
Common stock; $0.001 par value; 200,000,000 shares authorized;	96,099
96,098,850 issued and outstanding	

Additional paid- in capital	10,421,766
Accumulated deficit	(12,842,313)
Total stockholders' deficit	(2,324,448)
	$567,592

The accompanying notes are an integral part of these financial statements.

NIGHTHAWK SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THREE MONTHS ENDED MARCH 31, 2007 AND 2006

(unaudited)

	THREE MONTHS ENDED MARCH 31,	
	2007	**2006**
Revenue	$212,021	141,387
Cost of revenues	126,104	98,812
Gross profit	85,917	42,575
Selling, general and administrative expense	711,334	757,220
Loss from operations	(625,417)	(714,645)
Interest expense:		
Related parties	480	684
Other	491,405	600,352
	491,885	601,036
Net loss	(1,117,302)	(1,315,681)
Net loss per basic and diluted common share	($0.01)	($0.02)
Weighted average number of common shares outstanding		
basic and diluted	90,083,937	58,219,769

The accompanying notes are an integral part of these financial statements.

NIGHTHAWK SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS DEFICIT

THREE MONTHS ENDED MARCH 31, 2007

(unaudited)

	Common stock		Additional	Accumulated	
	Shares	Amount	paid-in capital	deficit	Total
Balances, December 31, 2006	85,681,150	$ 85,681	$ 9,719,022	$ (11,725,011)	$ 1,920,308
Common stock issued upon exercise of puts, including commissions	9,647,034	9,647	607,505		617,152
Common stock issued for note conversion	770,666	771	26,973		27,744
Stock-based compensation, vesting of options			68,266		68,266
Net loss				(1,117,302)	(1,117,302)
Balance as of March 31, 2007	96,098,850	$ 96,099	$ 10,421,766	$ (12,842,313)	$ 2,324,448

The accompanying notes are an integral part of these financial statements.

5

NIGHTHAWK SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

THREE MONTHS ENDED MARCH 31, 2007 AND 2006

(unaudited)

	THREE MONTHS ENDED MARCH 31,	
	2007	**2006**
Cash flows from operating activities:		
Net loss	($1,117,302)	($1,315,681)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,535	2,384
Employee options vested	68,266	2,988
Loan discounts and warrants	-	111,250
Amortization of discount on debt	278,066	153,269
Common stock issued for consulting services	120,000	177,000
Common stock issued for interest	-	88,109
Shares issued as incentives on notes payable	73,866	193,192
Note payable issued for consulting	-	24,850
Changes in assets and liabilities:		
Decrease in accounts receivable	83,857	3,795
(Increase) decrease in inventories	444	(80,955)
(Increase) decrease in prepaid expenses	31,227	(2,756)
Increase (decrease) in accounts payable	(7,334)	7,598
Increase in accrued expenses	186,242	29,841
Total adjustments	837,169	710,565
Net cash used in operating activities	(280,133)	(605,116)
Cash flows from investing activities:		
Purchases of furniture, fixtures and equipment	(959)	(8,861)
Net cash used in investing activities	(959)	(8,861)
Cash flows from financing activities:		
Payments on notes payable, related parties	(407)	(448)
Proceeds from notes payable, other	-	635,000
Payments on notes payable, other	(152,028)	(1,880)
Payments on line of credit	(100)	-
Net proceeds from the issuance of common stock	251,261	-

Net cash provided by financing activities	98,726	632,672
Net (decrease) increase in cash	(182,366)	18,695
Cash, beginning balance	270,910	91,205
Cash, ending balance	$88,544	$109,900

The accompanying notes are an integral part of these financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

THREE MONTHS ENDED MARCH 31, 2007 AND 2006

(unaudited)

(CONTINUED)

Supplemental disclosures of cash flow information:	**MARCH 31,**	
	2007	**2006**
Cash paid for interest	$7,024	$8,269
Supplemental disclosure of non-cash investing and financing activities:		
Common shares issued as incentive interest on notes payable		$148,880
Common shares issued for consulting agreements		$237,000
Common shares issued as payments on notes payable, other	$398,373	$1,205,334
Conversion of accrued expenses to common stock	$ -	$35,000
Conversion of notes payable to common stock	$27,744	

The accompanying notes are an integral part of these financial statements.

NIGHTHAWK SYSTEMS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

THREE MONTHS ENDED MARCH 31, 2007 AND 2006

1. ORGANIZATION, GOING CONCERN AND MANAGEMENT'S PLANS

INTERIM FINANCIAL STATEMENTS

The accompanying financial statements of Nighthawk Systems, Inc. (the Company) have been prepared in accordance with the instructions to quarterly reports on Form 10-QSB. In the opinion of Management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in financial position at March 31, 2007, and for all periods presented have been made. Certain information and footnote data necessary for fair presentation of financial position and results of operations in conformity with accounting principles generally accepted in the United States of America have been condensed or omitted. It is therefore suggested that these financial statements be read in conjunction with the summary of significant accounting policies and notes to financial statements included in the Company s Annual Report on Form 10-KSB. The results of operations for the quarter ended March 31, 2007, are not necessarily an indication of operating results for the full year.

ORGANIZATION

The Company designs and manufactures intelligent wireless power control products that enable simultaneous activation or de-activation of multiple assets or systems on demand. Nighthawk's installed customer base includes major electric utilities, internet service providers and fire departments in over 40 states. Nighthawk's products also enable custom message display, making them ideal for use in traffic control and emergency notification situations. Nighthawk products enable customers to wirelessly extend their reach, allowing them to turn on, off or reboot remotely located equipment at any time, from anywhere. These products allow for intelligent control by interpreting instructions sent via wireless media, and executing the instructions by 'switching' the electrical current that powers the device, system or process. Nighthawk's products can be activated individually, in pre-defined groups, or en masse, and for specified time periods with a simple click of a mouse or by dialing a telephone number.

The financial statements of the Company also include its non-operating subsidiary, Perergine Control Technologies, Inc. Intercompany accounts and transactions have been eliminated in consolidation.

GOING CONCERN AND MANAGEMENT'S PLANS

The Company incurred a net loss of approximately $1.1 million during the three month period ended March 31, 2007 and had negative working capital of approximately $2.6 million and a stockholders' deficit of approximately $2.3 million as of March 31, 2007. The Company s ability to continue as a going concern depends on the success of management s plans to overcome these conditions and ultimately achieve profitability and positive cash flows from operations Although no assurance can be given that such plans will be successfully implemented, management's plans to address these concerns include:

- Raising working capital through additional borrowings.
- Raising equity funding through sales of the Company's common stock.
- Implementation of the Company s sales and marketing plans.

In 2004, the Company signed an investment agreement with Dutchess Private Equities, II, L.P. ("Dutchess") under which Dutchess agreed to purchase up to $10.0 million in common stock from the Company, at the Company's discretion, over a three year period, subject to certain limitations including the Company's then current trading volume (Note 3). Although the amount and timing of specific cash infusions available under the entire financing arrangement cannot be predicted with certainty, the arrangement represents a contractual commitment by Dutchess to provide funds to the Company. Since entering into the arrangement with Dutchess, the Company has utilized the arrangement to obtain enough cash to cover its operating cash flow deficits on a monthly basis. Although no assurance may be given that it will be able to do so, the Company expects to be able to continue to access funds under this arrangement to help it fund near-term and long-term sales and marketing efforts, and to cover cash flow deficiencies.

The accompanying financial statements do not include any adjustments relating to the recoverability and classification of assets or the amounts of liabilities that might be necessary should the Company be unsuccessful in implementing these plans, or otherwise be unable to continue as a going concern.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No.48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement 109 (FIN 48) which clarifies the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 is a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return. If an income tax position exceeds a more likely than not (greater than 50%) probability of success upon tax audit, the company will recognize an income tax benefit in its financial statements. Additionally, companies are required to accrue interest and related penalties, if applicable, on all tax exposures consistent with jurisdictional tax laws. The Company adopted FIN 48 for the fiscal year beginning January 1, 2007. The Company did not have any unrecognized tax benefits and there was no effect on The Company s financial condition or results of operations as a result of implementing FIN 48. The Company files income tax returns in the U.S. federal and state of Colorado jurisdictions. The Company is no longer subject to tax examinations for years before 2004, and management does not believe there will be any material changes in the Company s unrecognized tax positions over the next 12 months. The Company recognizes interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of the date of adoption of FIN 48, the Company did not have any accrued interest or penalties associated with any unrecognized tax benefits, nor was any interest expense recognized by the Company during the quarter related to unrecognized tax benefits. The Company s effective tax rate differs from the federal statutory rate primarily due to non-deductible expenses and is offset somewhat by state tax credits.

2. SIGNIFICANT ACCOUNTING POLICIES

CONCENTRATIONS

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade accounts receivable. Receivables arising from sales to customers are not collateralized and, as a result, management continually monitors the financial condition and its relationships with its customers to reduce the risk of loss. The maximum loss that might be sustained if customer receivables are not collected is limited to the carrying amount of the accounts receivable, net of the allowance for doubtful accounts. Approximately $36,451 of this balance, or 43%, was from three customers, $25,794 of which was collected subsequent to March 31, 2007.

During the three months ended March 31, 2007, two customers accounted for approximately 29% and 11% of total revenue, respectively. During the three months ended March 31, 2006 , three customers accounted for approximately 10%,

12% and 14% of total revenue, respectively.

During the three months ended March 31, 2007, the Company's two largest suppliers accounted for approximately 12% and 58%, respectively, of the Company's purchases of pre-manufactured component materials. During the three months ended March 31, 2006, the Company's three largest suppliers accounted for approximately 14%, 19% and 47%, respectively, of the Company's purchases of pre-manufactured component materials. As the pre-manufactured components are a crucial integral component of the Company's product, the loss of one or more of the Company's major suppliers could have an adverse effect on the Company's ability to maintain production of its products on a cost effective basis in the future.

NET LOSS PER SHARE

Basic net loss per share is computed by dividing the net loss applicable to common stockholders by the weighted-average number of shares of common stock outstanding for the year. Diluted net loss per share reflects the potential dilution that could occur if dilutive securities were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company, unless the effect of such inclusion would reduce a loss or increase earnings per share. For each of the periods presented in the accompanying financial statements, the effect of the inclusion of dilutive hares would have resulted in a decrease in loss per share. Accordingly, the weighted average shares outstanding have not been adjusted for dilutive shares.

3. NOTES PAYABLE

At March 31, 2007, notes payable consist of the following:

unsecured; interest at prime rate plus 5.5% (13.99% at March 31, 2007); due on demand
unsecured; interest at 23.99%, revolving

ble to stockholder, 8% interest rate, in default as of the date of this report, collateralized by all assets of the Company(1)
holder, 8% interest rate, in default as of the date of this report, collateralized by all assets of the Company (1)

financial institution, 18.24% interest rate, interest and principal due monthly through November 2008

able to Dutchess; substantially all notes at 10% interest; maturing between December 2009 and

discount of $882,129

1) During the quarter ended March 31, 2007, the Company paid $150,000 to the stockholder. The Company and the stockholder remain in discussions as of the date of this report to either convert the remaining notes to common stock of the Company or to extend the terms.

All of the notes payable to Dutchess at March 31, 2007, contain a clause calling for an early redemption penalty of 20%. In addition, although Dutchess has not provided any indication it will do so, each of the debenture agreements contain a provision under which Dutchess may request the Company to make amortizing payments on a monthly basis in an amount to be determined by the Company and Dutchess. As such, the total amount of debentures outstanding is classified as a current liability.

The total amount of discount amortized to interest expense during the quarters ended March 31, 2007 and 2006 was $278,066 and $153,269, respectively.

During the quarter ended March 31, 2007, approximately $27,744 of debentures were converted into 770,666 shares of the Company s common stock. Total interest expense during the 2007 quarter related to the Dutchess debentures, which included amortization of the discount and $80,998 of early redemption penalties was $489,022, which represented an effective interest rate of 82%. Total interest expense during the 2006 quarter related to the Dutchess debentures, which included amortization of the discount and $36,250 of early redemption penalties was $591,287, which represented an effective interest rate of 100%.

4. STOCKHOLDERS' DEFICIT

COMMON STOCK

During the quarter ended March 31, 2007, the Company issued Dutchess 3,661,529 shares of common stock in exchange for cash of $251,261 and 5,985,505 shares of common stock in order to reduce the amount of convertible debt and accrued interest owed to them by $398,373. The Company accrued $32,482 in commissions related to these transactions. Dutchess also converted $27,744 of a convertible debenture into 770,666 shares of common stock during the period.

STOCK-BASED COMPENSATION

The estimated fair value of options granted during the quarters ended March 31, 2007 and 2006, were calculated using the following estimated weighted average assumptions:

		2007		**2006**
Stock options granted		4,450,000		150,000
Weighted-average exercise price	$	0.07	$	0.10
Weighted-average grant date fair value	$	0.041	$	0.064
Assumptions:				
Expected volatility		1.273%		1.256%
Expected term (in years)		1-2 years		2 years
Risk-free interest rate		4.50%		4.50%
Dividend yield		0%		0%

Most of the employee options vest over 3 years, which is considered to be the requisite service period. Stock options issued in exchange for consultant services vest over the period defined in the contract. During the three month period ended March 31, 2007, two employees, including the Company s Chief Executive Officer, were granted a total of 3,500,000 options, one third of which vested immediately, one third of which vest on June 30, 2007 and one third of which vest on December 31, 2007. The Company s board member was also awarded 500,000 options, half of which vested immediately, and half of which vest in January 2008.

The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term forfeitures is distinct from cancellations or expirations and represents only the unvested portion of the surrendered option.

The Company currently expects, based on an analysis of historical forfeitures that approximately 82% of our options will actually vest, and therefore have applied a forfeiture rate of 18% per year to all unvested options as of December 31, 2006. This analysis will be re-evaluated periodically and the forfeiture rate will be adjusted as necessary. Ultimately, the actual expense recognized over the vesting period will only be for those shares that vest.

Expected volatilities are based on the historical volatility of the price of our common stock. The expected term of options is derived based on the sum of the vesting term plus the original option term, divided by two.

A summary of stock option activity of options to employees and directors for the three months ended March 31, 2007, is presented below:

	Shares Under Option	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at January 1, 2007	8,710,000	$ 0.11		$
Granted	4,450,000	0.07		
Exercised				
Forfeited	(100,000)	0.01		
Outstanding at March 31, 2007	13,060,000	$ 0.10	9.0	$ 437,500
Exercisable at March 31, 2007	9,226,666	$ 0.11	8.0	$ 285,333

Based upon the Company's experience approximately 82% of the above stock options are expected to vest in the future, under their terms. As of March 31, 2007, there were 3,833,334 nonvested options outstanding that had a weighted average exercise price of $0.07 and a weighted average grant date fair value of $0.045.

The aggregate intrinsic value in the table above represents the total intrinsic value (the difference between our closing stock price on March 31, 2007 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders, had all option holders been able to and in fact, had exercised their options on March 31, 2007.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

FORWARD-LOOKING STATEMENTS

Discussions and information in this document, which are not historical facts, should be considered forward-looking statements. With regard to forward-looking statements, including those regarding the potential revenues from increased sales, and the business prospects or any other aspect of Nighthawk Systems, Inc.'s business, actual results and business performance may differ materially

from that projected or estimated in such forward-looking statements. Nighthawk Systems, Inc. ("the Company") has attempted to identify in this document certain of the factors that it currently believes may cause actual future experience and results to differ from its current expectations. Differences may be caused by a variety of factors, including but not limited to, adverse economic conditions, entry of new and stronger competitors, inadequate capital and the inability to obtain funding from third parties.

The following information should be read in conjunction with the unaudited condensed consolidated financial statements included herein which are prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information.

GENERAL

The Company designs and manufactures intelligent remote monitoring and power control products that are easy to use, inexpensive and can remotely control virtually any device from any location. Our proprietary, wireless products are ready to use upon purchase, so they are easily installed by anyone, regardless of technical ability, and are also easily integrated into third-party products, systems and processes. They allow for intelligent control by interpreting instructions sent via paging and satellite media, and executing the instructions by 'switching' the electrical current that powers the device, system or process. Our intelligent products can be activated individually, in pre-defined groups, or en masse, and for specified time periods with a simple click of a mouse or by dialing a telephone number.

Our products have been uniquely designed and programmed to be simple and ready to use upon purchase by anyone, almost anywhere, at affordable prices. As such, it is the Company's goal to have its products become commonplace, accepted and used by businesses and consumers alike in their daily routines.

We save consumers and businesses time, effort and expense by eliminating the need for a person to be present when and where an action needs to be taken. By utilizing existing wireless technology, we give our users the flexibility to move their application from place to place, without re-engineering their network. Currently, most commercial control applications utilize telephone lines, which tether the system to a single location and have associated installation and monthly charges. Our products make companies more profitable by eliminating installation costs and monthly charges for telephone lines, and allow for remote control of unmanned or remote locations that may operate on traditional electrical power, or solar or battery generated power.

Applications for our intelligent products include, but are not limited to:

- Rebooting remotely located computer equipment
- Remote switching of residential power
- Managing power on an electrical grid
- Activation/deactivation of alarm and warning devices
- Displaying or changing a digital or printed message or warning sign
- Turning pumps on or off
- Turning heating or cooling equipment on or off

Companies both large and small are seeking ways to save money and lower the risk of liability by replacing processes that require human intervention with processes that can be controlled remotely without on-site human intervention. Today, the remote control of industrial or commercial assets and processes is performed mainly through the use of telephone-line based systems. Opportunities

exist for companies that provide intelligent wireless solutions, as telephone lines are expensive and limited in availability and function. Nighthawk's products are wireless, and can be designed to work with a variety of wireless media. The number of applications for wireless remote control is virtually limitless. The Company has identified primary markets (Utility, IT Professional, Traffic Control), as well as secondary markets (Irrigation, Outdoor Advertising, Oil/Gas, Security) for its products.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In July 2006, the FASB issued FASB Interpretation No.48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement 109 (FIN 48) which clarifies the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 is a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return. If an income tax position exceeds a more likely than not (greater than 50%) probability of success upon tax audit, the company will recognize an income tax benefit in its financial statements. Additionally, companies are required to accrue interest and related penalties, if applicable, on all tax exposures consistent with jurisdictional tax laws. We adopted FIN 48 for the fiscal year beg9inning January 1, 2007. We did not have any unrecognized tax benefits and there was no effect on our financial condition or results of operations as a result of implementing FIN 48. We file income tax returns in the U.S. federal and state of Colorado jurisdictions. We are no longer subject to tax examinations for years before 2004. We do not believe there will be any material changes in our unrecognized tax positions over the next 12 months. Our policy is that we recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of the date of adoption of FIN 48, we did not have any accrued interest or penalties associated with any unrecognized tax benefits, nor was any interest expense recognized during the quarter related to unrecognized tax benefits. Our effective tax rate differs from the federal statutory rate primarily due to non-deductible expenses and is offset somewhat by state tax credits.

COMPARISON OF THE THREE MONTHS ENDED MARCH 31, 2007 AND MARCH 31, 2006

Revenue

The components of revenue and their associated percentages of total revenues, for the three months ended March 31, 2007 and 2006 are as follows:

	2007		2006		Change %	Change $
Revenues:						
Rebooting products	$ 31,285	15%	$ 47,070	33%	(33%)	$(15,785)
Logic boards	84,570	40%	17,465	12%	385%	67,105
Utility products	63,512	29%	47,998	34%	32%	15,514
Emergency notification products	13,639	6%	17,815	13%	(23%)	(4,176)
Hydro 1	1,125	1%	-	-	100%	1,125
Airtime sales	14,304	7%	8,045	6%	78%	6,259
Other product	1,823	1%	1,392	1%	32%	431
Freight	1,763	1%	1,602	1%	10%	161
Total revenues	$212,021	100%	$141,387	100%	50%	$ 70,634

Revenues for the three-month period ended March 31, 2007 were $212,021 as compared to $141,387 for the prior year, an increase of 50% between periods. During the first quarter of 2007, the Company received in excess of $300,000 in orders from customer sm but a delay in receiving component parts from a supplier prevented the Company from building and shipping approximately $100,000 in additional utility products during the quarter. The Company expects these orders and new orders to be completed during the second quarter of 2007. Sales of the Company s logic boards increased 385% between the periods presented, largely due to a sale of $61,625 in units to a single customer. Sales of the Company's rebooting products decreased approximately $16,000 from period to period, and sales of emergency notification products decreased approximately $5,000 between the periods presented. The Company did not spend as much marketing effort and resources in these areas as it did with its utility products. The Company has identified enhancements that it would like to make to its rebooting products during 2007 before it focuses additional marketing dollars on the products.

Airtime sales, generated on a recurring basis by the Company by reselling access to wireless networks, increased 78% from the first quarter of 2006 to the 2007 period. The increase in airtime revenues is a direct result of more of the Company s units being purchased and placed into operation by customers.

Cost of revenues includes parts and pre-manufactured components used to assemble our products as well as allocated overhead for production personnel and facilities costs. Cost of goods sold increased by $27,292 or 28% to $126,104 for the three months ended March 31, 2006 from $98,812 for the corresponding period of the prior year but decreased as a percentage of revenues between the periods from 70% in 2005 to 59% in 2006. As a result, the Company's gross margin increased between the periods from 30% to 41% and the Company produced twice as many gross margin dollars in the 2007 period as it did in the 2006 period. This increase is almost entirely due to the increase in sales of the higher margin logic board units during the first quarter of 2007.

Selling, general and administrative expenses for the three months ended March 31, 2007 decreased by $45,886 or 6% from the three-month period ended March 31, 2006. This decrease was due primarily to decreases in expenses associated with consulting and public relations firms. These decreases more than offset approximately $68,000 in noncash expenses associated with the award of options to employees, as well as to a Company board member, during the period.

Interest expense decreased $108,947 or 18% between the three-month periods presented. During the first quarter of 2006, six Duthcess debentures and notes were paid off prior to their maturity date. When this occurs, the Company expenses any unamortized discount associated with the debt being paid off, as well as any unamortized expense associated with incentive shares issued with the debt and any early redemption penalties. During the first quarter of 2006, the Company recognized interest expense of approximately $153,000 related to the beneficial conversion feature of debentures, as well as approximately $192,000 in interest expense related for the value of incentive shares issued to Dutchess in exchange for money loaned to the Company. The Company also recognized approximately $77,000 in interest expense during the 2006 period in early redemption penalties on debentures that were paid off during the period. During the first quarter of 2007, only one Dutchess debenture was paid off prior to its maturity date.

The net loss to common shareholders for the three-month period ended March 31, 2007 was $1,117,302 compared to $1,315,681 for the three-month period ended March 31, 2006.

LIQUIDITY AND CAPITAL RESOURCES

The Company s financial statements for three months ended March 31, 2007 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business.

The Report of our Independent Registered Public Accounting Firm on the Company's financial statements as of and for the year ended December 31, 2006 includes a "going concern" explanatory paragraph which means that the auditors expressed substantial doubt about the Company's ability to continue as a going concern. Although no assurance can be given that such plans will be successfully implemented, management's plans to address these concerns include:

- Raising working capital through additional borrowings.
- Raising equity funding through sales of the Company's common stock.
- Continued implementation of the Company s sales and marketing plans to generate

  additional cash flows from operations.

In August 2004, the Company signed a financing arrangement with Dutchess Private Equities, II, L.P. ("Dutchess") under which the Company received $250,000 in exchange for a convertible debenture during August 2004. The Company also signed an investment agreement under which Dutchess agreed to purchase up to $10.0 million in common stock from the Company, at the Company's discretion, over the next three years, subject to certain limitations including the Company's then current trading volume. Although the amount and timing of specific cash infusions available under the entire financing arrangement cannot be predicted with certainty, the arrangement represents a contractual commitment by Dutchess to provide funds to the Company. Since entering into the arrangement with Dutchess, the Company has utilized the arrangement to obtain enough cash to cover its operating cash flow deficits on a monthly basis.

As a result of higher margin sales made during the first quarter of 2006, combined with decreased selling, general and administrative expenses, cash used in operating activities was approximately $267,000, less than half of the amount of cash used in operating activities during the 2006 period. Cash proceeds from the exercise of puts to Dutchess totaled $251,261 during the 2007 period. Using cash on hand, the Company paid down $150,000 in debt owed to one of its creditors during the 2007 period.

The Company issued 5,985,505 shares to Dutchess during the quarter ended March 31, 2007 which was used to pay down $398,373 in debt and accrued interest during the period.

Until the Company is able to generate positive cash flows from operations in an amount sufficient to cover its current liabilities and debt obligations as they become due, it will remain reliant on borrowing funds from or selling equity to Dutchess or other parties to meet those obligations. Although the amount and timing of specific cash infusions available under the entire financing arrangement cannot be predicted with certainty, the arrangement represents a contractual commitment by Dutchess to provide funds to the Company.

ITEM 3. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures:

The Company's management, including the Company's principal executive officer and principal accounting and financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the three-month period ended March 31, 2007, the period covered by the Quarterly Report on Form 10-QSB. Based upon that evaluation, the Company's principal executive officer and principal financial and accounting officer have concluded that the disclosure controls and procedures were effective as of March 31, 2007 to provide reasonable assurance that material information relating to the Company is made known to management including the CEO.

There were no changes in the Company's internal control over financial reporting that occurred during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None

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

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

The Company is in default on two loans from Mr. Revesz, a former board member, as of the date of this report and is in discussions to extend the maturity dates on those notes.

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS

(a) Exhibits

31.1 Certification of H. Douglas Saathoff, Chief Executive Officer and Principal Financial and Accounting Officer, pursuant to Rule 13A-14 or 15D-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certification pursuant to the 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K.

None

SIGNATURES

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

NIGHTHAWK SYSTEMS, INC.
(Registrant)

Date: May 15, 2007

By: /s/ H. Douglas Saathoff
H. Douglas Saathoff
Chief Executive Officer
Principal Accounting and Financial Officer