

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

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For The Quarterly Period Ended February 28, 2017

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

COMMISSION FILE NUMBER 000-27688

SURGE COMPONENTS, INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of
incorporation or organization)

11-2602030

(I.R.S. Employer
Identification No.)

95 East Jefryn Blvd., Deer Park, New York

(Address of principal executive offices)

11729

(Zip code)

Issuer's telephone number: **(631) 595-1818**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

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

As of April 6, 2017 there were 5,224,431 outstanding shares of the Registrant's Common Stock, \$.001 par value.

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PART I - FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS.**

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

	February 28, 2017 (unaudited)	November 30, 2016
ASSETS		
Current assets:		
Cash	\$ 7,250,109	\$ 7,120,601
Accounts receivable - net of allowance for doubtful accounts of \$159,976 and \$159,976	4,033,848	5,558,808
Inventory, net	3,058,909	2,929,570
Prepaid expenses and income taxes	136,040	144,824
Deferred income taxes	318,253	304,887
Total current assets	14,797,159	16,058,690
Fixed assets – net of accumulated depreciation and amortization of \$2,193,374 and \$2,185,540	87,334	81,974
Deferred income taxes	747,502	609,773
Other assets	13,384	13,384
Total assets	\$ 15,645,379	\$ 16,763,821

See notes to consolidated financial statements

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets
(Continued)

	February 28, 2017 (unaudited)	November 30, 2016
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 2,957,156	\$ 3,237,592
Accrued expenses and taxes	958,048	1,544,882
Accrued salaries	533,825	431,111
Total current liabilities	4,449,029	5,213,585
Deferred rent	38,748	39,962
Total liabilities	4,487,777	5,253,547
Commitments and contingencies		
Shareholders' equity		
Preferred stock - \$.001 par value stock, 5,000,000 shares authorized:		
Series A - 260,000 shares authorized, none outstanding, non-voting, convertible, redeemable.		
Series B - 200,000 shares authorized, none outstanding, voting, convertible, redeemable.		
Series C - 100,000 shares authorized, 10,000 and 10,000 shares issued and outstanding, redeemable, convertible, and a liquidation preference of \$5 per share		
	10	10
Series D - 75,000 shares authorized, none issued or outstanding, voting, convertible, redeemable.		
Common stock - \$.001 par value stock, 75,000,000 shares authorized, 10,224,431 and 10,224,431 shares issued and outstanding	10,224	10,224
Additional paid-in capital	23,702,310	23,702,310
Accumulated deficit	(12,554,942)	(12,202,270)
Total shareholders' equity	11,157,602	11,510,274
Total liabilities and shareholders' equity	\$ 15,645,379	\$ 16,763,821

See notes to consolidated financial statements.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Operations
(unaudited)

	Three Months Ended	
	February 28, 2017	February 29, 2016
Net sales	\$ 5,665,147	\$ 6,316,011
Cost of goods sold	4,255,794	4,659,999
Gross profit	1,409,353	1,656,012
Operating expenses:		
Selling and shipping expenses	560,776	525,846
General and administrative expenses	1,329,063	998,902
Depreciation and amortization	7,834	7,816
Total operating expenses	1,897,673	1,532,564
(Loss) Income before other income and income taxes	(488,320)	123,448
Other income:		
Investment income	2,968	1,325
Other income	2,968	1,325
(Loss) Income before income taxes	(485,352)	124,773
Income taxes (benefits)	(135,180)	30,302
Net (Loss) income	\$ (350,172)	\$ 94,471
Dividends on preferred stock	2,500	2,500
Net (Loss) income available to common shareholders	\$ (352,672)	\$ 91,971
Net (Loss) income per share available to common shareholders:		
Basic	\$ (.03)	\$.01
Diluted	\$ (.03)	\$.01
Weighted Shares Outstanding:		
Basic	10,224,431	9,999,125
Diluted	10,224,431	10,115,350

See notes to consolidated financial statements.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows
(unaudited)

	Three Months Ended	
	February 28, 2017	February 29, 2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (Loss) Income	\$ (350,172)	\$ 94,471
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:		
Depreciation and amortization	7,834	7,816
Stock compensation expense	-	-
Deferred income taxes	(151,095)	(2,436)
Allowance for doubtful accounts	-	8,440
CHANGES IN OPERATING ASSETS AND LIABILITIES:		
Accounts receivable	1,524,960	679,426
Inventory	(129,339)	220,052
Prepaid expenses and income taxes	8,784	(8,045)
Other assets	-	-
Accounts payable	(280,436)	(869,343)
Deferred rent	(1,214)	(355)
Accrued expenses	(486,620)	(214,002)
NET CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES	142,702	(83,976)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of fixed assets	(13,194)	(1,520)
NET CASH FLOWS USED IN INVESTING ACTIVITIES	\$ (13,194)	\$ (1,520)

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows
(unaudited)
(Continued)

	Three Months Ended	
	February 28, 2017	February 29, 2016
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repurchase of Common Stock	\$ -	\$ -
Proceeds from exercising stock options	-	-
NET CASH FLOWS PROVIDED BY FINANCING ACTIVITIES	-	-
NET CHANGE IN CASH	129,508	(85,496)
CASH AT BEGINNING OF PERIOD	7,120,601	7,169,118
CASH AT END OF PERIOD	\$ 7,250,109	\$ 7,083,622
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Income taxes paid	\$ 9,611	\$ 3,355
Interest paid	\$ -	\$ -
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Accrued dividends on preferred stock	\$ 2,500	\$ 2,500

See notes to consolidated financial statements.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE A – ORGANIZATION, DESCRIPTION OF COMPANY’S BUSINESS AND BASIS OF PRESENTATION

Surge Components, Inc. (“Surge”) was incorporated in the State of New York and commenced operations on November 24, 1981 as an importer of electronic products, primarily capacitors and discrete semi-conductors selling to customers located principally throughout North America. On June 24, 1988, Surge formed Challenge/Surge Inc. (“Challenge”), a wholly-owned subsidiary to engage in the sale of electronic component products and sounding devices from established brand manufacturers to customers located principally throughout North America.

In May 2002, Surge and an officer of Surge founded and became sole owners of Surge Components, Limited (“Surge Limited”), a Hong Kong corporation. Under current Hong Kong law, Surge Limited is required to have at least two shareholders. Surge owns 999 shares of the outstanding common stock and the officer of Surge owns 1 share of the outstanding common stock. The officer of Surge has assigned his rights regarding his 1 share to Surge. Surge Limited started doing business in July 2002. Surge Limited operations have been consolidated with the Company. Surge Limited is responsible for the sale of Surge’s products to customers located in Asia.

On August 31, 2010, the Company changed its corporate domicile by merging into a newly-formed corporation, Surge Components, Inc. (Nevada), which was formed in the State of Nevada for that purpose. Surge Components Inc. is the surviving entity. The number of common stock shares authorized for issuance was increased to 75,000,000 shares.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(1) Principles of Consolidation:

The consolidated financial statements include the accounts of Surge, Challenge, and Surge Limited (collectively the “Company”). All material intercompany balances and transactions have been eliminated in consolidation.

The accompanying interim consolidated financial statements have been prepared without audit, in accordance with the instructions to Form 10-Q for interim financial reporting pursuant to the rules and regulations of the Securities and Exchange Commission.

The results and trends in these interim consolidated financial statements for the three months ended February 28, 2017 and February 29, 2016 may not be representative of those for the full fiscal year or any future periods.

(2) Accounts Receivable:

Trade accounts receivable are recorded at the net invoice value and are not interest bearing. The Company considers receivables past due based on the payment terms. The Company reviews its exposure to accounts receivable and reserves specific amounts if collectability is no longer reasonably assured. The Company also reserves a percentage of its trade receivable balance based on collection history and current economic trends that might impact the level of future credit losses. The Company re-evaluates such reserves on a regular basis and adjusts its reserves as needed. Based on the Company’s operating history and customer base, bad debts to date have not been material.

(3) Revenue Recognition:

Revenue is recognized for products sold by the Company when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable, collectability is reasonably assured and title and risk of loss have been transferred to the customer. This occurs when product is shipped from the Company’s warehouse.

For direct shipments, revenue is recognized when product is shipped from the Company’s supplier. The Company has a long term supply agreement with one of our suppliers. The Company purchases the merchandise from the supplier and has the supplier directly ship the merchandise to the customer through a freight forwarder. Title passes to the customer upon the merchandise being received by a freight forwarder. Direct shipments were approximately \$458,000 and \$771,000 for the three months ended February 28, 2017 and February 29, 2016 respectively.

The Company also acts as a sales agent to certain customers in North America for one of its suppliers. The Company reports these commissions as revenues in the period earned. Commission revenue totaled \$46,774 and \$67,554 for the three months ended February 28, 2017 and February 29, 2016 respectively.

The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(3) Revenue Recognition (continued):

The Company and its subsidiaries currently have agreements with several distributors. There are no provisions for the granting of price concessions in any of the agreements. Revenues under these distribution agreements were approximately \$1,114,000 and \$2,080,000 for the three months ended February 28, 2017 and February 29, 2016 respectively.

(4) Inventories:

Inventories, which consist solely of products held for resale, are stated at the lower of cost (first-in, first-out method) or market. Products are included in inventory when the Company obtains title and risk of loss on the products, primarily when shipped from the supplier. Inventory in transit principally from foreign suppliers at February 28, 2017 was \$1,289,000. The Company, at February 28, 2017, has a reserve against slow moving and obsolete inventory of \$226,874. From time to time the Company's products are subject to legislation from various authorities on environmental matters.

(5) Depreciation and Amortization:

Fixed assets are recorded at cost. Depreciation is generally calculated on a straight line method and amortization of leasehold improvements is provided for on the straight-line method over the estimated useful lives of the various assets as follows:

Furniture, fixtures and equipment	5 - 7 years
Computer equipment	5 years
Leasehold Improvements	Estimated useful life or lease term, whichever is shorter

Maintenance and repairs are expensed as incurred while renewals and betterments are capitalized.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(6) Concentration of Credit Risk:

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of accounts receivables. The Company maintains substantially all of its cash balances in a limited number of financial institutions. At February 28, 2017 and November 30, 2016, the Company's uninsured cash balances totaled \$4,685,114 and \$4,550,807, respectively.

(7) Income Taxes:

The Company's deferred income taxes arise primarily from the differences in the recording of net operating losses, allowances for bad debts, inventory reserves and depreciation expense for financial reporting and income tax purposes. A valuation allowance is provided when it has been determined to be more likely than not that the likelihood of the realization of deferred tax assets will not be realized. See Note I.

The Company follows the provisions of the Accounting Standards Codification topic, ASC 740, "Income Taxes" (ASC 740). There have been no unrecognized tax benefits and, accordingly, there has been no effect on the Company's financial condition or results of operations as a result of ASC 740.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company is no longer subject to U.S. federal tax examinations for years before fiscal years ending November 30, 2012, and state tax examinations for years before fiscal years ending November 30, 2011. Management does not believe there will be any material changes in our unrecognized tax positions over the next twelve months.

The Company's policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income expense. As of the date of adoption of ASC 740, there was no accrued interest or penalties associated with any unrecognized benefits, nor was any interest expense recognized during the three months ended February 28, 2017 and February 29, 2016.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)(8) Cash Equivalents:

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

(9) Use of Estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(10) Marketing and promotional costs:

Marketing and promotional costs are expensed as incurred and have not been material to date. The Company has contractual arrangements with several of its distributors which provide for cooperative advertising rights to the distributor as a percentage of sales. Cooperative advertising is reflected as a reduction in revenues and has not been material to date.

(11) Fair Value of Financial Instruments:

The carrying amount of cash balances, accounts receivable, accounts payable and accrued expenses approximate their fair value based on the nature of those items. Estimated fair values of financial instruments are determined using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret the market data used to develop the estimates of fair value, and accordingly, the estimates are not necessarily indicative of the amounts that could be realized in a current market exchange.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(12) Shipping Costs

The Company classifies shipping costs as a component of selling expenses. Shipping costs totaled \$1,413 and \$1,037 for the three months ended February 28, 2017 and February 29, 2016 respectively.

(13) Earnings Per Share

Basic earnings (loss) per share includes no dilution and is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. The difference between reported basic and diluted weighted-average common shares results from the assumption that all dilutive stock options and convertible preferred stock exercised into common stock. Dilutive securities are excluded from diluted weighted shares outstanding at February 28, 2017 since the Company had a net loss in the period and including the securities would be anti-dilutive. Total potentially dilutive shares excluded from diluted weighted shares outstanding at February 28, 2017 and February 29, 2016 totaled 635,438 and 519,213, respectively.

(14) Stock Based Compensation

Stock Based Compensation to Employees

The Company accounts for its stock-based compensation for employees in accordance with Accounting Standards Codification (“ASC”) 718. The Company recognizes in the statement of operations the grant-date fair value of stock options and other equity-based compensation issued to employees and non-employees over the related vesting period.

Stock Based Compensation to Other than Employees

The Company accounts for equity instruments issued in exchange for the receipt of goods or services from other than employees in accordance with ASC 718. Costs are measured at the estimated fair market value of the consideration received or the estimated fair value of the equity instruments issued, whichever is more reliably determinable. The value of equity instruments issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE C – FIXED ASSETS

Fixed assets consist of the following:

	February 28, 2017	November 30, 2016
Furniture and Fixtures	\$ 327,971	\$ 327,971
Leasehold Improvements	962,637	956,637
Computer Equipment	990,100	982,906
Less-Accumulated Depreciation	(2,193,374)	(2,185,540)
Net Fixed Assets	<u>\$ 87,334</u>	<u>\$ 81,974</u>

Depreciation and amortization expense for the three months ended February 28, 2017 and February 29, 2016 was \$7,834 and \$7,816, respectively.

NOTE D – LINE OF CREDIT

In February 2017, the Company obtained a line of credit with a bank for up to \$3,000,000 (the "Credit Line"). Borrowings under the Credit Line accrue interest at the greater of the prime rate or the LIBOR rate plus two percent (2.0%). As of February 28, 2017 there were no borrowings under the Credit Line.

NOTE E – ACCRUED EXPENSES

Accrued expenses consist of the following:

	February 28, 2017	November 30, 2016
Commissions	\$ 200,812	\$ 281,888
Preferred Stock Dividends	134,069	131,569
Interest	-	-
Other accrued expenses	180,076	321,465
Accrued Professional Fees	443,091	809,960
	<u>\$ 958,048</u>	<u>\$ 1,544,882</u>

NOTE F – RETIREMENT PLAN

In June 1997, the Company adopted a qualified 401(k) retirement plan for all full-time employees who are twenty-one years of age and have completed twelve months of service. The plan allows total employee contributions of up to fifteen percent (15%) of the eligible employee's salary through salary reduction. The Company makes a matching contribution of twenty percent (20%) of each employee's contribution for each dollar of employee deferral up to five percent (5%) of the employee's salary. Net assets for the plan, as estimated by Union Central, Inc., which maintains the plan's records, were approximately \$1,229,000 at November 30, 2016. Pension expense for the three months ended February 28, 2017 and February 29, 2016 was \$1,289 and \$1,030, respectively.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE G – SHAREHOLDERS' EQUITY[1] Preferred Stock:

In February 1996, the Company amended its Certificate of Incorporation to authorize the issuance of 1,000,000 shares of preferred stock in one or more series. In August 2010, the number of preferred shares authorized for issuance was increased to 5,000,000 shares.

In January 2000, the Company authorized 260,000 shares of preferred stock as Non-Voting Redeemable Convertible Series A Preferred Stock ("Series A Preferred Stock"). None of the Series A Preferred Stock is outstanding as of February 28, 2017.

In November 2000, the Company authorized 200,000 shares of preferred stock as Voting Redeemable Convertible Series B Preferred Stock ("Series B Preferred Stock"). None of the Series B Preferred Stock is outstanding as of February 28, 2017.

In November 2000, the Company authorized 100,000 shares of preferred stock as Non-Voting Redeemable Convertible Series C Preferred Stock ("Series C Preferred"). Each share of Series C Preferred is automatically convertible into 10 shares of our common stock upon shareholder approval. If the Series C Preferred were converted into common stock on or before April 15, 2001, these shares were entitled to cumulative dividends at the rate of \$.50 per share per annum commencing April 15, 2001 payable on June 30 and December 31 of each year. In November 2000, 70,000 shares of the Series C Preferred were issued in payment of financial consulting services to its investment banker and a shareholder of the Company. In April 2001, 8,000 shares of the Series C Preferred were repurchased and cancelled.

In April 2002, in connection with a Mutual Release, Settlement, Standstill and Non-Disparagement Agreement among other provisions, certain investors transferred back to the Company 252,000 shares of common stock, 19,300 shares of Series C preferred stock, and certain warrants, in exchange for \$225,000. These repurchased shares were cancelled.

In February 2006, the Company settled with a shareholder to repurchase 10,000 shares of Series C Preferred plus accrued dividends for \$50,000.

Pursuant to exchange agreements dated as of March 14, 2011, 9,000 shares of Series C Preferred were returned to the Company for cancellation in exchange for 112,500 shares of common stock.

In October 2014, 2,000 shares of Series C Preferred were converted into 20,000 shares of common stock.

In April 2015, the Company entered into a settlement agreement with a shareholder pursuant to which 7,500 shares of Series C Preferred were returned to the Company for cancellation in exchange for 110,000 shares of common stock plus \$65,000 for accrued dividends and legal fees and expenses.

In July 2015, 4,200 shares of Series C Preferred were exchanged for 42,000 shares of common stock and \$29,838 in accrued dividends.

Dividends aggregating \$134,069 have not been paid for the semi-annual periods ended December 31, 2001 through the semi-annual payment due December 31, 2016. The Company has accrued these dividends. At February 28, 2017, there are 10,000 shares of Series C Preferred issued and outstanding.

In October 2016, the Company authorized 75,000 shares of preferred stock as Voting Non-Redeemable Convertible Series D Preferred Stock ("Series D Preferred"). None of the Series D Preferred Stock is outstanding as of February 28, 2017.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE G – SHAREHOLDERS’ EQUITY (Continued)

[2] 2010 Incentive Stock Plan

In March 2010, the Company adopted, and in April 2010 the shareholders ratified, the 2010 Incentive Stock Plan (“2010 Incentive Plan”). The 2010 Incentive Plan provides for the grant of options to officers, employees, directors or consultants to the Company to purchase an aggregate of 1,500,000 common shares.

Activity in the 2010 Incentive Plan for the three months ended February 28, 2017 is summarized as follows:

	<u>Shares</u>	<u>Weighted Average Exercise Price</u>
Options outstanding December 1, 2016	352,000	\$ 0.87
Options issued in the three months ended February 28, 2017	-	\$ -
Options exercised in the three months ended February 28, 2017	-	\$ -
Options cancelled in the three months ended February 28, 2017	-	\$ -
Options outstanding at February 28, 2017	<u>352,000</u>	<u>\$ 0.87</u>
Options exercisable at February 28, 2017	<u>352,000</u>	<u>\$ 0.87</u>

[3] 2015 Equity Incentive Plan

In November 2015, the Company adopted and its shareholders ratified, the 2015 Equity Incentive Plan (“2015 Incentive Plan”). The 2015 Incentive Plan provides for the grant of awards to officers, employees, directors or consultants to the Company to purchase up to an aggregate of 1,500,000 shares of common stock.

In May 2016 a total of 99,151 shares were issued to the Company’s officers as part of their 2015 bonus compensation under the 2015 Incentive Plan.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE G – SHAREHOLDERS' EQUITY (Continued)Stock Compensation

In April 2016, the Company awarded one employee director 67,901 shares of its common stock and another employee director 31,250 shares of its common stock under the 2015 Incentive Plan as part of their 2015 bonus. The Company recorded a cost of \$74,363 relating to the issuance of these shares.

In October 2016 one employee director exercised options to acquire 50,000 shares of common stock at \$0.82 per share and 62,500 shares of common stock at \$0.80 per share. In October 2016, one employee director exercised options to acquire 25,000 shares of common stock at \$0.82 per share and 45,938 shares of common stock at \$0.80 per share.

The intrinsic value of the exercisable options at February 28, 2017 totaled \$180,960. At February 28, 2017 the weighted average remaining life of the stock options is 1.43 years. At February 28, 2017, there was no unrecognized compensation cost related to the stock options granted under the Company's incentive plans.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE G – SHAREHOLDERS' EQUITY (Continued)

[4] Authorized Repurchase:

In November 2015, the Board of Directors authorized the Company to purchase up to \$500,000 of common stock in the open market or in privately negotiated transactions. Pursuant to such authority and pursuant to Rule 10b-18 under the Securities Exchange Act of 1934, as amended ("Exchange Act"), as of February 28, 2017 a total of 57,283 shares were repurchased for approximately \$48,300. In January 2017, the Company terminated its repurchase program.

[5] Compensation of Directors

Compensation for each non-employee director is \$2,500 per month (and \$3,500 per month for a non-employee director that serves as the chairman of more than two committees of the Board of Directors).

NOTE H – SETTLEMENT AGREEMENT

On or about October 31, 2016, Michael D. Tofias and Bradley P. Rexroad (collectively, the "Stockholders") filed a Complaint and Motion for Preliminary Injunction against the Company in the eighth Judicial District Court, Clark County, Nevada, Case No. A-16-745890-B, seeking relief including, inter alia, immediate inspection of certain books and records and a 60-day postponement of the scheduled annual meeting of stockholders ("Annual Meeting"). On November 16, 2016, after the Company postponed the Annual Meeting and provided certain books and records to the Stockholders, the Stockholders filed an Amended Complaint, which named all members of the Board as defendants and alleged that the directors had breached their fiduciary duty to the Stockholders. On December 1, 2016, following a hearing, the Court denied the request for a preliminary injunction. On December 22, 2016, the Company entered into a settlement agreement (the "Settlement Agreement") with the Stockholders.

The Settlement Agreement provides that:

- the Stockholders irrevocably withdraw their director nominations for the Board and stockholder proposals for the Company's annual meeting of stockholders for fiscal year 2015 (the "Meeting");
- the Stockholders will vote all of their shares of common stock of the Company in accordance with the Board's recommendations with respect to the election of the Board's director nominees, the ratification of the Company's independent registered public accounting firm for the fiscal year ending November 30, 2016 (the "2017 Meeting") and the ratification of the Company's rights plan;
- the Company will hold the Meeting on January 5, 2017 and will hold its annual meeting of stockholders for fiscal year 2016 by December 29, 2017;
- the Board and the Stockholders will identify a mutually acceptable independent director to join the Board as a Class C director by February 28, 2017 and the Board will include that new director among its director nominees for the 2017 Meeting;
- the Company will not make any stock or option grants or grant any other non-cash compensation to its current officers and directors until December 23, 2017;
- the Company will take all steps to (i) change its state of incorporation from the State of Nevada to the State of Delaware and (ii) declassify the Board on a rolling basis by June 30, 2017, and the Company will convene a special meeting of stockholders of the Company for the purpose of approving such actions, at which meeting the Stockholders and the Insiders will vote all of their shares of common stock of the Company in favor of such actions;
- the Company will commence an issuer tender offer to all of its stockholders to repurchase at least 5.0 million shares of its common stock at a price of \$1.43 per share (the "Tender Offer"), which Tender Offer will be completed by March 15, 2017;

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

- until the day after the announcement of the completion of the Tender Offer, the Board will be composed of no more than seven individuals;
- the Stockholders will tender all of the shares of common stock of the Company that they hold beneficially or of record in the Tender Offer, subject to limited exceptions;
- the Company’s officers and directors will not participate in the Tender Offer and will not transfer or sell any of their shares until six months after the Tender Offer is completed;
- subject to certain conditions, if the Tender Offer is not completed by March 15, 2017, the Company will (i) appoint the Stockholders to the Board as Class A directors with terms expiring at the Company’s annual meeting of stockholders for fiscal year 2018 (the “2019 Meeting”) and (ii) reduce the size of the Board to six directors, including the Stockholders;
- the Stockholders will withdraw with prejudice their lawsuit against the Company and the Insiders pending in the State of Nevada; and
- the Stockholders will be subject to customary standstill provisions until the termination of the Settlement Agreement.

Pursuant to the Settlement Agreement, the Company also agreed to reimburse the expenses of the Stockholders associated with their investment in the Company, including their proxy solicitation and litigation costs, in an amount not to exceed \$300,000.

The Settlement Agreement terminates on the date that is 15 business days prior to the deadline for the submission of director nomination and stockholder proposals for the 2019 Meeting.

NOTE I – INCOME TAXES

Deferred income taxes reflect 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 using the enacted tax rates in effect in the years in which the differences are expected to reverse.

The Company’s deferred income taxes are comprised of the following:

	February 28, 2017	November 30, 2016
Deferred Tax Assets		
Net operating loss	\$ 4,343,920	\$ 4,208,030
Allowance for bad debts	49,276	49,276
Inventory	86,742	100,446
Deferred Rent	15,476	15,961
Depreciation	148,943	149,172
Total deferred tax assets	4,644,357	4,522,885
Valuation allowance	(3,578,602)	(3,608,225)
Total	\$ 1,065,755	\$ 914,660

The valuation allowance for the deferred tax assets relates principally to the uncertainty of the utilization of deferred tax assets and was calculated in accordance with the provisions of ASC 740, which requires that a valuation allowance be established or maintained when it is “more likely than not” that all or a portion of deferred tax assets will not be realized. The valuation allowance decreased by approximately \$29,600 during the three months ended February 28, 2017. This valuation is based on management estimates of future taxable income. Although the degree of variability inherent in the estimates of future taxable income is significant and subject to change in the near term, management believes, that the estimate is adequate. The estimated valuation allowance is continually reviewed and as adjustments to the allowance become necessary, such adjustments are reflected in the current operations.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE I – INCOME TAXES (CONTINUED)

The Company's income tax expense consists of the following:

	Three Months Ended	
	February 28, 2017	February 29, 2016
Current:		
Federal	\$ -	\$ 5,436
States	16,725	27,302
	<u>16,725</u>	<u>32,738</u>
Deferred:		
Federal	(125,230)	(1,934)
States	(26,675)	(502)
	<u>(151,905)</u>	<u>(2,436)</u>
Provision for income taxes	<u>\$ (135,180)</u>	<u>\$ 30,302</u>

The Company files a consolidated income tax return with its wholly-owned subsidiaries and has net operating loss carryforwards of approximately \$11,020,000 for federal and state purposes, which expire through 2020. A reconciliation of the difference between the expected income tax rate using the statutory federal tax rate and the Company's effective rate is as follows:

	Three Months Ended	
	February 28, 2017	February 29, 2016
U.S Federal Income tax statutory rate	(34)%	34%
Valuation allowance	16%	(18)%
State income taxes	(9)%	8%
Other	-	-
Effective tax rate	<u>(27)%</u>	<u>24%</u>

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE J – RENTAL COMMITMENTS

The Company leases its office and warehouse space through 2020 from a corporation that is controlled by officers/shareholders of the Company (“Related Company”). Annual minimum rental payments to the Related Company approximated \$173,000 for the year ended November 30, 2016, and increase at the rate of three per cent per annum throughout the lease term.

Pursuant to the lease, rent expense charged to operations differs from rent paid because of scheduled rent increases. Accordingly, the Company has recorded deferred rent. Rent expense is calculated by allocating to rental payments, including those attributable to scheduled rent increases, on a straight line basis, over the lease term.

In June 2015, the Company renewed its lease to rent office space and a warehouse in Hong Kong for two years. Annual minimum rental payments for this space are approximately \$58,500.

The Company’s future minimum rental commitments at February 28, 2017 are as follows:

Three Months Ended		
February 28,		
2018	\$	195,062
2019	\$	184,055
2020	\$	108,608
	<u>\$</u>	<u>487,725</u>

Net rental expense for the three months ended February 28, 2017 and February 29, 2016 were \$77,435 and \$77,435 respectively, of which \$64,034 and \$63,174 respectively, was paid to the Related Company.

SURGE COMPONENTS, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE K – EMPLOYMENT AND OTHER AGREEMENTS

In February 2016, the Company entered into revised employment agreements with two officers of the Company. Pursuant to these agreements, the base salary for one officer is \$275,000 and the base salary for the other officer is \$225,000. The agreements continue until terminated by either party.

The Company’s compensation committee may award these officers with bonuses and will review the base salary amounts for each of the officers on an annual basis to determine if any changes to the base salary amounts need to be made and may also award these officers with annual bonuses. Pursuant to the employment agreements, the officers are prohibited from engaging in activities which are competitive with those of the Company during their employment with the Company and for one year following termination. If the agreement is terminated other than for cause, the officer would be entitled to any and all base salary earned through the date of termination, accrued but unused vacation, all vested equity, and bonus amounts payable to the officer through the date of termination. The officers would also be entitled to receive paid an additional thirty-six months of annual compensation equal to the average of his base salary and bonus for the three calendar years prior to the date of termination, payable in accordance with the Company’s regular payroll practice over a 52-week period.

NOTE L – MAJOR CUSTOMERS

The Company had one customer who accounted for 11% of net sales for the three months ended February 28, 2017 and two customers who accounted for 12% and 13% of net sales for the three months ended February 29, 2016. The Company had no customers who accounted for 10% of accounts receivable at February 28, 2017 and February 29, 2016.

NOTE M – MAJOR SUPPLIERS

During the three months ended February 28, 2017 and February 29, 2016, there was one foreign supplier accounting for 54% and 54% of total inventory purchased.

The Company purchases substantially all of its products overseas. For the three months ended February 28, 2017, the Company purchased 56% of its products from Taiwan, 16% from Hong Kong, 29% from elsewhere in Asia and less than 1% overseas outside of Asia. The Company purchases the balance of its products in the United States.

NOTE N – EXPORT SALES

The Company’s export sales were as follows:

	Three Months Ended	
	February 28, 2017	February 29, 2016
Canada	695,555	1,099,473
China	766,068	1,176,748
Other Asian Countries	358,421	174,096
South America	88,527	84,059
Europe	278,109	78,250

Revenues are attributed to countries based on location of customer.

NOTE O – SUBSEQUENT EVENTS

[1] Tender Offer

In March 2017, the Company completed a tender offer by purchasing for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000.

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

The following discussion contains forward-looking statements. All statements other than statements of historical facts contained herein, including statements regarding our future results of operations and financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

In some cases, forward-looking statements can be identified by terms such as "may," "will," "should," "expects," "plans," "anticipates," "could," "intends," "target," "projects," "contemplates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of these terms or other similar words. These statements are only predictions. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our business, financial condition and results of operations. We discuss many of the risks in greater detail under the heading "Risk Factors" in our Annual Report on Form 10-K. Also, these forward-looking statements represent our estimates and assumptions only as of the date of the filing of this report. Except as required by law, we assume no obligation to update any forward-looking statements for events or circumstances occurring after the date of the filing of this report.

Overview

The Company operates with two sales groups, Surge Components ("Surge") and Challenge Electronics ("Challenge"). Surge is a supplier of electronic products and components. These products include capacitors, which are electrical energy storage devices, and discrete semiconductor components, such as rectifiers, transistors and diodes, which are single function low power semiconductor products that are packaged alone as compared to integrated circuits such as microprocessors. The products sold by Surge are typically utilized in the electronic circuitry of diverse products, including, but not limited to, automobiles, audio products, temperature control products, lighting products, energy related products, computer related products, various types of consumer products, garage door openers, household appliances, power supplies and security equipment. These products are sold to both original equipment manufacturers, commonly referred to as OEMs, who incorporate them into their products, and to distributors of the lines of products we sell, who resell these products within their customer base. These products are manufactured predominantly in Asia by approximately sixteen independent manufacturers. We act as the master distribution agent utilizing independent sales representative organizations in North America to sell and market the products for one such manufacturer pursuant to a written agreement. When we act as a sales agent, our supplier who sold the product to the customer that we introduced to our supplier pays us a commission. The amount of the commission is determined on a sale by sale basis depending on the profit margin of the product. Commission revenue totaled \$46,774 and \$67,554 for the three months ended February 28, 2017 and February 29, 2016 respectively.

Challenge is engaged in the sale of electronic components. In 1999, Challenge began as a division to sell audible components. We have been able to increase the types of products that we sell because some of our suppliers introduced new products, and we also located other products from new suppliers. Our core products include buzzers, speakers, microphones, resonators, alarms, chimes, filters, and discriminators. We now also work with our suppliers to have our suppliers customize many of the products we sell for many customers through the customers' own designs and those that we work with our suppliers to have our suppliers redesign for them at our suppliers' factories. We have a design engineer on our staff with more than thirty years of experience with these types of products, who works with our suppliers on such redesigns. We are continually looking to expand the line of products that we sell. In 2015, we hired a junior engineer to assist with the introduction of a new micro controller product line. We sell these products through independent representatives that earn a commission on the products we sell. We are also working with local, regional, and national distributors to sell these products to local accounts in every state.

The Company has a Hong Kong office to effectively handle the transfer business from United States customers purchasing and manufacturing in Asia after designing the products in the United States. This office has strengthened the Company's global position, improving our capabilities and service to our customer base.

The electronic components industry continues to change, from one of strong demand to now one of challenged demand. This challenged demand can be attributed to a slowdown in global growth as well as a slowdown in the forecast of retail sales in North America. Management expects 2017 to continue with the challenged demand for components that it experienced in 2016.

The world of business is constantly changing because of "disruptors," which are significant changes in traditional business practices that did not previously exist. For example, customers are moving to centralized purchasing from regional purchasing and are stretching their payment terms. These changes also include customers moving their manufacturing operations from North America to Asia, and the trend of globalization. This trend makes business more complicated and costly for the Company. The Company must have a presence in Asia to service and further develop the business. For these reasons, we established Surge Ltd., our Asia subsidiary. Currency fluctuations also have an effect on doing business outside of North America. As we pay our suppliers in U.S dollars, whenever the currency exchange rate between U.S dollars and other countries' currencies change, a supplier is receiving more or less U.S. dollars for its currency, and therefore may raise the prices it charges us accordingly. Customers have moved to reduce their supply chain, which could adversely affect the Company. In some market segments, demand for electronic components have decreased, and in other segments, the demand is still strong. Some technologies have become obsolete, while customers develop new products using different kinds of components. Management expects 2017 to be a year of change and challenge. These challenges could affect the Company in negative ways, possibly reducing sales and or profitability. In order for the Company to grow, we will depend on, among other things, the continued growth of the electronics and semiconductor industries, our ability to withstand intense price competition, our ability to obtain new customers, our ability to retain and attract sales and other key personnel in order to expand our marketing capabilities, our ability to secure adequate sources of products, which are in demand on commercially reasonable terms, our success in executing and managing growth, including monitoring an expanded level of operations and systems, controlling costs, the availability of adequate financing, and our ability to deal successfully, with new and future disruptors.

Critical Accounting Policies

Accounts Receivable

The allowance for doubtful accounts is based on the Company's assessment of the collectability of specific customer accounts and an assessment of international, political and economic risk as well as the aging of the accounts receivable. If there is a change in actual defaults from the Company's historical experience, the Company's estimates of recoverability of amounts due could be affected and the Company would adjust the allowance accordingly.

Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable, collectability is reasonably assured and title and risk of loss have been transferred to the customer. This occurs when product is shipped from the Company's warehouse. For direct shipments from our suppliers to our customer, revenue is recognized when product is shipped from the Company's supplier. The Company acts as a sales agent for certain customers buying direct from one of its suppliers. The Company reports these commissions as revenues in the period earned.

The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses.

Inventory Valuation

Inventories are recorded at the lower of cost or market. Write-downs of inventories to market value are based on stock rotation, historical sales requirements and obsolescence as well as in the changes in the backlog. Reserves required for obsolescence were not material in any of the periods in the financial statements presented. If market conditions are less favorable than those projected by management, additional write-downs of inventories could be required. For example, each additional 1% of obsolete inventory would reduce operating income by approximately \$33,000.

The Company does not have price protection agreements with any of its vendors and assumes the risk of changes in the prices of its products. The Company does not believe there is a significant risk with regards to the lack of price protection agreements since many of its inventory items are purchased to fulfill purchase orders received.

Income Taxes

We have made a number of estimates and assumptions relating to the reporting of a deferred income tax asset to prepare our financial statements in accordance with generally accepted accounting principles. These estimates have a significant impact on our valuation allowance relating to deferred income taxes. Our estimates could materially impact the financial statements.

Results of Operations

Consolidated net sales for the three months ended February 28, 2017 decreased by \$650,864 or 10.3%, to \$5,665,147 as compared to net sales of \$6,316,011 for the three months ended February 29, 2016. We attribute the decrease to certain of the Company's customers having excess inventory in the first part of the first quarter of 2017. This resulted in those customers delaying ordering products from us during the three months ended February 28, 2017. We expect sales for those customers to increase starting in the three months ended May 31, 2017. We also attribute the decrease in net sales to a downward trend in market demand for our products due to adverse market conditions in certain areas of the world, reducing these customers' demand for our products. Even though these adverse market conditions exist, certain of our customers are doing well which has resulted in an increase in sales to Europe and other areas of Asia for the three months ended February 28, 2017. The Company expects these market conditions to continue through the first half of 2017. The Company also attributes a portion of the decrease in sales to senior management's attention being diverted due to the recent proxy contest and related settlement.

Our gross profit for the three months ended February 28, 2017 decreased by \$246,659 to \$1,409,353, or 14.9%, as compared to \$1,656,012 for the three months ended February 29, 2016. Gross margin as a percentage of net sales decreased to 24.9% for the three months ended February 28, 2017 compared to 26.2% for the three months ended February 29, 2016. The Company attributed the decrease in gross profit margin and percentage to sales mostly to existing customers with a lower profit margin in the three months ended February 28, 2017. Profit margins in 2016 and 2017 have been impacted as a result of certain of our customers, who are some of the biggest buyers of components, demanding the lowest prices for our products. Some of them further demand periodic price reductions on a quarterly or semi-annual basis, as opposed to annual fixed pricing. We work with electronic manufacturing service subcontractor customers who manufacture products for other customers who do not have their own manufacturing operations. At times we are not able to recover these price reductions from our suppliers. The Company has agreements with these subcontractor customers to provide periodic cost reductions through rebates in the amount of 5%. These reductions only affect future shipments of our products, and does not affect existing orders. These reductions can have a negative impact on our profit margins since it reduces the amount of commissions we can earn. Even though this rebate can impact the Company's gross profit margin, these subcontractor customers represent very significant potential growth for the Company, because they can help the Company become an approved supplier at the customers they manufacture for, and they purchase our components for these customers. It would be very difficult for the Company to achieve business at these customers without the help of these subcontractor customers.

Selling and shipping expenses for the three months ended February 28, 2017 was \$560,776, an increase of \$34,930, or 6.6%, as compared to \$525,846 for the three months ended February 29, 2016. We attribute the increase to hiring additional salespeople to grow the business, as well as increases in selling expenses such as commissions, printing and freight, offset by a decrease in travel and entertainment expenses.

General and administrative expenses for the three months ended February 28, 2017 was \$1,329,063, an increase of \$330,161, or 33.1%, as compared to \$998,902 for the three months ended February 29, 2016. The increase is due primarily to the costs of approximately \$37,000 that the Company incurred during the proxy contest and related settlement with certain shareholders of the Company and costs of approximately \$218,000 that the Company incurred in connection with the tender offer completed by the Company in March 2017. . Other increases are due to the hiring of additional employees and increased costs for public company expenses, health insurance and consulting expenses as well as increases in temporary help expense, and partially offset by decreases in general insurance, bad debt expenses and promotional expenses.

Depreciation expense for the three months ended February 28, 2017 was \$7,834, an increase of \$18, or less than one percent, as compared to \$7,816 for the three months ended February 29, 2016.

Investment income for the three months ended February 28, 2017 was \$2,968, an increase of \$1,643, or 124% compared to \$1,325 for the three months ended February 29, 2016.

Tax expense for the three months ended February 28, 2017 was \$(135,180), a decrease of \$165,482 or 546% as compared to a tax expense of \$30,302 for the three months ended February 29, 2016. The decrease is a result of our net loss for the 2017 period and management's revised estimate of future taxable income and the related impact on the reported deferred tax. The change in the valuation allowance is based on management estimates of future taxable income. The degree of variability inherent in the estimates of future taxable income is significant and subject to change in the near term. The Company reviews its estimates of future taxable income in each reporting period and adjustments to the valuation allowance are reflected in the current operations.

As a result of the foregoing, net loss for the three months ended February 28, 2017 was \$350,172, compared to net income of \$94,471 for the three months ended February 29, 2016.

Liquidity and Capital Resources

As of February 28, 2017 we had cash of \$7,250,109, and working capital of \$10,348,130. In March 2017, the Company completed a tender offer purchasing for cash 5,000,000 shares of its common stock at a price of \$1.43 per share. In February 2017, the Company obtained a line of credit with a bank for up to \$3,000,000. We believe that our working capital levels and available financing are adequate to meet our operating requirements during the next twelve months.

During the three months ended February 28, 2017, we had net cash flow provided by operating activities of \$142,702, as compared to net cash flow used in operating activities of \$(83,976) for the three months ended February 29, 2016. The increase in cash flow operating activities resulted from a decrease in accounts receivable, as partially offset by the net loss and an increase in cash used by inventory, accounts payable and accrued expenses.

We had net cash flow used in investing activities of \$(13,194) for the three months ended February 28, 2017, as compared to net cash flow used in investing activities of \$(1,520) for the three months ended February 29, 2016. We attribute the change to the Company purchasing new equipment during the three months ended February 28, 2017.

We had net cash flow provided by financing activities totaling \$0 during the three months ended February 28, 2017 as compared to \$0 for the three months ended February 29, 2016.

As a result of the foregoing, the Company had a net increase in cash of \$129,508 for the three months ended February 28, 2017, as compared to a net decrease in cash of \$85,496 for the three months ended February 29, 2016.

In November 2015, the Board of Directors authorized the Company to purchase up to \$500,000 of shares of common stock in the open market or in privately negotiated transactions. The Company repurchased 57,283 shares to date pursuant to such authority. In January 2017, the Board of Directors terminated the repurchase program.

In February 2017, the Company completed a tender offer whereby it purchased for cash 5,000,000 shares of its common stock, at a price of \$1.43 per share, or \$7,150,000. In February 2017, the Company obtained a line of credit of up to \$3.0 million for working capital. As of February 28, 2017 there were no borrowings under the Credit Line. In March 2017, the Company borrowed \$1,000,000 under the line of credit. The Company anticipated the line of credit to be utilized for working capital purposes and to be repaid out of expected cash flows to be generated from operations.

The table below sets forth our contractual obligations, including long-term debt, operating leases and other long-term obligations, as of February 28, 2017:

Contractual Obligations	Total	Payments due			
		0 – 12 Months	13 – 36 Months	37 – 60 Months	More than 60 Months
Long-term debt	\$ -	\$ -	\$ -	\$ -	\$ -
Operating leases	\$ 487,725	195,062	292,663	-	-
Total obligations	\$ 487,725	\$ 195,062	\$ 292,663	\$ -	\$ -

Inflation

In the past two fiscal years, inflation has not had a significant impact on our business. However, any significant increase in inflation and interest rates could have a significant effect on the economy in general and, thereby, could affect our future operating results.

Off Balance Sheet Arrangements

We do not have any off balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934, as amended (“Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (“Commission”). Ira Levy, the Company’s principal executive officer and principal financial officer has evaluated the effectiveness of the Company’s disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of February 28, 2017 and has concluded that, as of such date, our disclosure controls and procedures were effective.

Changes in Internal Controls

During the three months ended February 28, 2017, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION**ITEM 1. LEGAL PROCEEDINGS.**

There are no legal proceedings to which the Company or any of its property is the subject.

ITEM 1A. RISK FACTORS.

Not applicable.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.*Share Repurchases*

Share repurchase activity during the three months ended February 28, 2017 was as follows:

Periods	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs ⁽¹⁾
December 1, 2016 to December 31, 2016:	-	\$ -	-	\$ 451,649
January 1, 2017 to January 31, 2017:	-	\$ -	-	\$ 451,649
February 1, 2017 to February 28, 2017:	-	-	-	\$ 451,649
Total	-	\$ -	-	\$ 451,649

(1) In November 2015, the Company's Board of Directors authorized a program to repurchase up to \$500,000 of the Company's common stock. The Company's share repurchase program did not obligate the Company to acquire any specific number of shares. Under the program, shares may be repurchased in privately negotiated and/or open market transactions pursuant to Rule 10b-18 under the Exchange Act, including under plans complying with Rule 10b5-1 under the Exchange Act. In January 2017, the Company terminated the repurchase program.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

Exhibit Number	Description
10.1	Business Loan Agreement, dated February 22, 2017, between Surge Components Inc. and Citibank N.A.
10.2	Promissory Note, dated February 22, 2017, issued to Citibank N.A.
31.1	Certification by principal executive officer and principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification by principal executive officer and principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: April 14, 2017

SURGE COMPONENTS, INC.

By: /s/ Ira Levy

Name: Ira Levy

Title: Chief Executive Officer
(Principal Executive Officer,
Principal Financial Officer and
Principal Accounting Officer)

Exhibit 10.1

BUSINESS LOAN AGREEMENT (ASSET BASED)

Borrower: Surge Components, Inc.
95 East Jefryn Boulevard
Deer Park, NY 11729

Lender: Citibank, N.A.
6801 Colwell Boulevard
Irving, TX 75039

THIS BUSINESS LOAN AGREEMENT (ASSET BASED) dated February 22, 2017, is made and executed between Surge Components, Inc. (“Borrower”) and Citibank, N.A. (“Lender”) on the following terms and conditions. Borrower has received prior commercial loans from Lender or has applied to Lender for a commercial loan or loans or other financial accommodations, including those which may be described on any exhibit or schedule attached to this Agreement. Borrower understands and agrees that: (A) in granting, renewing, or extending any Loan, Lender is relying upon Borrower’s representations, warranties, and agreements as set forth in this Agreement; (B) the granting, renewing, or extending of any Loan by Lender at all times shall be subject to Lender’s sole judgment and discretion; and (C) all such Loans shall be and remain subject to the terms and conditions of this Agreement.

TERM. This Agreement shall be effective as of February 22, 2017, and shall continue in full force and effect until such time as all of Borrower’s Loans in favor of Lender have been paid in full, including principal, interest, costs, expenses, attorneys’ fees, and other fees and charges, or until such time as the parties may agree in writing to terminate this Agreement.

LINE OF CREDIT. Lender agrees to make Advances to Borrower from time to time from the date of this Agreement to the Expiration Date, provided the aggregate amount of such Advances outstanding at any time does not exceed the Borrowing Base. Within the foregoing limits, Borrower may borrow, partially or wholly prepay, and reborrow under this Agreement as follows:

Conditions Precedent to Each Advance. Lender’s consideration of Borrower’s request to make any Advance to or for the account of Borrower under this Agreement is subject to the following conditions precedent, with all documents, instruments, opinions, reports, and other Items required under this Agreement to be in form and substance satisfactory to Lender:

- (1) Lender shall have received evidence that this Agreement and all Related Documents have been duly authorized, executed, and delivered by Borrower to Lender.
- (2) Lender shall have received such opinions of counsel, supplemental opinions, and documents as Lender may request.
- (3) The security interests in the Collateral shall have been duly authorized, created, and perfected with first lien priority and shall be in full force and effect.
- (4) All guaranties required by Lender for the credit facility(ies) shall have been executed by each Guarantor, delivered to Lender, and be in full force and effect.
- (5) Lender, at its option and for its sole benefit, shall have conducted an audit of Borrower’s Accounts and Guarantor’s Accounts, Inventory, books, records, and operations, and Lender shall be satisfied as to their condition.
- (6) Borrower shall have paid to Lender all fees, costs, and expenses specified in this Agreement and the Related Documents as are then due and payable.
- (7) There shall not exist at the time of any Advance a condition which would constitute an Event of Default under this Agreement, and Borrower shall have delivered to Lender the compliance certificate called for in the paragraph below titled “Compliance Certificate.”
- (8) Lender to have received a fully executed Landlord waiver upon execution of this Agreement for 95 E Jefryn Blvd, Deer Park, NY 11729 in form and substance satisfactory to Lender.

Making Loan Advances. Advances under this credit facility, as well as directions for payment from Borrower’s accounts, may be requested orally or in writing by authorized persons. Lender may, but need not, require that all oral requests be confirmed in writing. Each Advance shall be conclusively deemed to have been made at the request of and for the benefit of Borrower (1) when credited to any deposit account of Borrower maintained with Lender or (2) when advanced in accordance with the instructions of an authorized person. Lender, at its option, may set a cutoff time, after which all requests for Advances will be treated as having been requested on the next succeeding Business Day. Under no circumstances shall Lender be required to make any Advance in an amount less than \$10,000.00.

Mandatory Loan Repayments. If at any time the aggregate principal amount of the outstanding Advances shall exceed the applicable Borrowing Base, Borrower, immediately upon written or oral notice from Lender, shall pay to Lender an amount equal to the difference between the outstanding principal balance of the Advances and the Borrowing Base. On the Expiration Date, Borrower shall pay to Lender in full the aggregate unpaid principal amount of all Advances then outstanding and all accrued unpaid interest, together with all other applicable fees, costs and charges, if any, not yet paid.

Loan Account. Lender shall maintain on Its books a record of account in which Lender shall make entries for each Advance and such other debits and credits as shall be appropriate in connection with the credit facility. Lender shall provide Borrower with periodic statements of Borrower’s account, which statements shall be considered to be correct and conclusively binding on Borrower unless Borrower notifies Lender to the contrary within thirty (30) days after Borrower’s receipt of any such statement which Borrower deems to be incorrect.

COLLATERAL. To secure payment of the Primary Credit Facility and performance of all other Loans, obligations and duties owed by Borrower to Lender, Borrower (and others, if required) shall grant to Lender Security Interests in such property and assets as Lender may require. Lender's Security Interests in the Collateral shall be continuing liens and shall include the proceeds and products of the Collateral, including without limitation the proceeds of any insurance. With respect to the Collateral, Borrower agrees and represents and warrants to Lender:

Perfection of Security Interests. Borrower agrees to execute all documents perfecting Lender's Security Interest and to take whatever actions are requested by Lender to perfect and continue Lender's Security Interests in the Collateral. Upon request of Lender, Borrower will deliver to Lender any and all of the documents evidencing or constituting the Collateral, and Borrower will note Lender's interest upon any and all chattel paper and instruments if not delivered to Lender for possession by Lender. Contemporaneous with the execution of this Agreement, Borrower will execute one or more UCC financing statements and any similar statements as may be required by applicable law, and Lender will file such financing statements and all such similar statements in the appropriate location or locations. Borrower hereby appoints Lender as its irrevocable attorney-in-fact for the purpose of executing any documents necessary to perfect or to continue any Security Interest. Lender may at any time, and without further authorization from Borrower, file a carbon, photograph, facsimile, or other reproduction of any financing statement for use as a financing statement. Borrower will reimburse Lender for all expenses for the perfection, termination, and the continuation of the perfection of Lender's security interest in the Collateral. Borrower promptly will notify Lender before any change in Borrowers name including any change to the assumed business names of Borrower. Borrower also promptly will notify Lender before any change in Borrower's Social Security Number or Employer identification Number. Borrower further agrees to notify Lender in writing prior to any change in address or location of Borrower's principal governance office or should Borrower merge or consolidate with any other entity.

Collateral Records. Borrower does now, and at all times hereafter shall, keep correct and accurate records of the Collateral, all of which records shall be available to Lender or Lenders representative upon demand for inspection and copying at any reasonable time. With respect to the Accounts, Borrower agrees to keep and maintain such records as Lender may require, including without limitation information concerning Eligible Accounts and Account balances and agings. Records related to Accounts (Receivables) are or will be located at Borrowers primary place of business. With respect to the Inventory, Borrower agrees to keep and maintain such records as Lender may require, including without limitation information concerning Eligible Inventory and records itemizing and describing the kind, type, quality, and quantity of Inventory, Borrower's Inventory costs and selling prices, and the daily withdrawals and additions to Inventory. Records related to Inventory are or will be located at Borrower's primary place of business. The above is an accurate and complete list of all locations at which Borrower keeps or maintains business records concerning Borrowers collateral.

Collateral Schedules. Concurrently with the execution and delivery of this Agreement, Borrower shall execute and deliver to Lender schedules of Accounts and Inventory and schedules of Eligible Accounts and Eligible Inventory in form and substance satisfactory to the Lender. Thereafter supplemental schedules shall be delivered according to the following schedule: With respect to Eligible Accounts, schedules shall be delivered as hereinafter provided. With respect to Eligible Inventory, schedules shall be delivered as hereinafter provided.

Representations and Warranties Concerning Accounts. With respect to the Accounts, Borrower represents and warrants to Lender (1) Each Account represented by Borrower to be an Eligible Account for purposes of this Agreement conforms to the requirements of the definition of an Eligible Account; (2) All Account information listed on schedules delivered to Lender will be true and correct, subject to immaterial variance; and (3) Lender, its assigns, or agents shall have the right at any time and at Borrower's expense to inspect, examine, and audit Borrower's records and to confirm with Account Debtors the accuracy of such Accounts.

Representations and Warranties Concerning inventory. With respect to the Inventory, Borrower represents and warrants to Lender (1) All Inventory represented by Borrower to be Eligible Inventory for purposes of this Agreement conforms to the requirements of the definition of Eligible Inventory; (2) All Inventory values listed on schedules delivered to Lender will be true and correct, subject to immaterial variance; (3) The value of the Inventory will be determined on a consistent accounting basis; (4) Except as agreed to the contrary by Lender in writing, all Eligible Inventory is now and at all times hereafter will be in Borrower's physical possession and shall not be held by others on consignment, sale on approval, or sale or return; (5) Except as reflected in the Inventory schedules delivered to Lender, all Eligible Inventory is now and at all times hereafter will be of good and merchantable quality, free from defects; (6) Eligible Inventory is not now and will not at any time hereafter be stored with a bailee, warehouseman, or similar party without Lender's prior written consent, and, in such event, Borrower will concurrently at the time of bailment cause any such bailee, warehouseman, or similar party to issue and deliver to Lender, in form acceptable to Lender, warehouse receipts in Lender name evidencing the storage of inventory; and (7) Lender, its assigns, or agents shall have the right at any time and at Borrower's expense to inspect and examine the Inventory and to check and test the same as to quality, quantity, value, and condition.

CONDITIONS PRECEDENT TO EACH ADVANCE. The request for the initial Advance and each subsequent Advance under this Agreement shall be subject to the fulfillment to Lender's satisfaction of ail of the conditions set forth in this Agreement and in the Related Documents.

Loan Documents. Borrower shall provide to Lender the following documents for the Loan: (1) the Note; (2) Security Agreements granting to Lender security interests in the Collateral; (3) financing statements and all other documents perfecting Lender's Security Interests; (4) evidence of insurance as required below; (5) guaranties; (6) together with all such Related Documents as Lender may require for the Loan; all in form and substance satisfactory to Lender and Lender's counsel.

Borrower's Authorization. Borrower shall have provided in form and substance satisfactory to Lender properly certified resolutions, duly authorizing the execution and delivery of this Agreement, the Note and the Related Documents. In addition, Borrower shall have provided such other resolutions, authorizations, documents and instruments as Lender or its counsel, may require.

Fees and Expenses Under This Agreement. Borrower shall have paid to Lender all fees, costs, and expenses specified in this Agreement and the Related Documents as are then due and payable.

Representations and Warranties. The representations and warranties set forth in this Agreement, in the Related Documents, and in any document or certificate delivered to Lender under this Agreement are true and correct.

No Event of Default. There shall not exist at the time of any Advance a condition which would constitute an Event of Default under this Agreement or under any Related Document.

Requesting Advances. Advances under this Agreement, as well as directions for payment from Borrower's accounts, may be requested (i) orally or in writing by Borrower, or (ii) by use of Lender's online banking system for Advances bearing or to bear interest at the Prime Rate or the Minimum Interest Rate, as such terms are defined in a Note providing for borrowing at such interest rates, pursuant to an online access agreement between Borrower and Lender. Lender may, but need not, require that all oral requests be confirmed in writing. Borrower agrees to be liable for all sums either (a) advanced in accordance with the instructions of an authorized person or online user, or (b) credited to any of Borrower's accounts with Lender.

REPRESENTATIONS AND WARRANTIES. Borrower represents and warrants to Lender, as of the date of this Agreement, as of the date of each disbursement of loan proceeds, as of the date of any renewal, extension or modification of any Loan, and at all times any Indebtedness exists:

Organization. Borrower is a corporation for profit which is, and except as permitted below, at all times shall be, duly organized, validly existing, and in good standing under and by virtue of the laws of the State of Nevada. Borrower is duly authorized to transact business in all other states in which Borrower is doing business, having obtained all necessary filings, governmental licenses and approvals for each state in which Borrower is doing business. Specifically, Borrower is, and at all times shall be, duly qualified as a foreign corporation in all states in which the failure to so qualify would have a material adverse effect on its business or financial condition. Borrower has the full power and authority to own its properties and to transact the business in which it is presently engaged or presently proposes to engage. Borrower maintains an office at 95 East Jeffry Boulevard, Deer Park, NY 11729. Unless Borrower has designated otherwise in writing, the principal office is the office at which Borrower keeps its books and records including its records concerning the Collateral. Provided Borrower notifies Lender prior to any change in the location of Borrower's state of organization, Borrower may convert to a Delaware corporation subject to Bank's receipt of (i) documentation satisfactory to Bank in its sole discretion demonstrating that after conversion, except for the state of its Incorporation, Borrower is the same Borrower as the Borrower prior to conversion, and (ii) any and all documents deemed necessary by the Bank to (a) maintain its perfected security interest in the Collateral and (b) ensure all agreements and documents executed by Borrower, any Guarantor and any Grantor in connection with the Loan, including but not limited to any guarantees, remain in full force and effect. Borrower will notify Lender prior to any change in Borrower's name. Borrower shall do all things necessary to preserve and to keep in full force and effect its existence, rights and privileges, and shall comply with all regulations, rules, ordinances, statutes, orders and decrees of any governmental or quasi-governmental authority or court applicable to Borrower and Borrower's business activities.

Assumed Business Names. Borrower has filed or recorded all documents or filings required by law relating to all assumed business names used by Borrower. Excluding the name of Borrower, the following is a complete list of all assumed business names under which Borrower does business: **None.**

Authorization. Borrower's execution, delivery, and performance of this Agreement and all the Related Documents have been duly authorized by all necessary action by Borrower and do not conflict with, result in a violation of, or constitute a default under (1) any provision of (a) Borrower's articles of incorporation or organization, or bylaws, or (b) any agreement or other instrument binding upon Borrower or (2) any law, governmental regulation, court decree, or order applicable to Borrower or to Borrower's properties.

Financial Information. Each of Borrower's financial statements supplied to Lender truly and completely disclosed Borrower's financial condition as of the date of the statement, and there has been no material adverse change in Borrower's financial condition subsequent to the date of the most recent financial statement supplied to Lender. Borrower has no material contingent obligations except as disclosed in such financial statements.

Legal Effect. This Agreement constitutes, and any Instrument or agreement Borrower is required to give under this Agreement when delivered will constitute legal, valid, and binding obligations of Borrower enforceable against Borrower in accordance with their respective terms.

Properties. Except as contemplated by this Agreement or as previously disclosed in Borrower's financial statements or in writing to Lender and as accepted by Lender, and except for property tax liens for taxes not presently due and payable, Borrower owns and has good title to all of Borrower's properties free and clear of all Security Interests, and has not executed any security documents or financing statements relating to such properties. All of Borrower's properties are titled in Borrower's legal name, and Borrower has not used or filed a financing statement under any other name for at least the last five (5) years.

Hazardous Substances. Except as disclosed to and acknowledged by Lender in writing, Borrower represents and warrants that: (1) During the period of Borrower's ownership of the Collateral, there has been no use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance by any person on, under, about or from any of the Collateral. (2) Borrower has no knowledge of, or reason to believe that there has been (a) any breach or violation of any Environmental Laws; (b) any use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance on, under, about or from the Collateral by any prior owners or occupants of any of the Collateral; or (c) any actual or threatened litigation or claims of any kind by any person relating to such matters. (3) Neither Borrower nor any tenant, contractor, agent or other authorized user of any of the Collateral shall use, generate, manufacture, store, treat, dispose of or release any Hazardous Substance on, under, about or from any of the Collateral; and any such activity shall be conducted in compliance with all applicable federal, state, and local laws, regulations, and ordinances, including without limitation all Environmental Laws. Borrower authorizes Lender and its agents to enter upon the Collateral to make such inspections and tests as Lender may deem appropriate to determine compliance of the Collateral with this section of the Agreement. Any inspections or tests made by Lender shall be at Borrower's expense and for Lender's purposes only and shall not be construed to create any responsibility or liability on the part of Lender to Borrower or to any other person. The representations and warranties contained herein are based on Borrower's due diligence in investigating the Collateral for hazardous waste and Hazardous Substances. Borrower hereby (1) releases and waives any future claims against Lender for indemnity or contribution in the event Borrower becomes liable for cleanup or other costs under any such laws, and (2) agrees to Indemnify, defend, and hold harmless Lender against any and all claims, losses, liabilities, damages, penalties, and expenses which Lender may directly or indirectly sustain or suffer resulting from a breach of this section of the Agreement or as a consequence of any use, generation, manufacture, storage, disposal, release or threatened release of a hazardous waste or substance on the Collateral. The provisions of this section of the Agreement, including the obligation to indemnify and defend, shall survive the payment of the Indebtedness and the termination, expiration or satisfaction of this Agreement and shall not be affected by Lender's acquisition of any interest in any of the Collateral, whether by foreclosure or otherwise.

Litigation and Claims. No litigation, claim, investigation, administrative proceeding or similar action (including those for unpaid taxes) against Borrower is pending or threatened, and no other event has occurred which may materially adversely affect Borrower's financial condition or properties, other than litigation, claims, or other events, if any, that have been disclosed to and acknowledged by Lender in writing.

Taxes. To the best of Borrower's knowledge, all of Borrower's tax returns and reports that are or were required to be filed, have been filed, and all taxes, assessments and other governmental charges have been paid in full, except those presently being or to be contested by Borrower in good faith in the ordinary course of business and for which adequate reserves have been provided.

Lien Priority. Unless otherwise previously disclosed to Lender in writing, Borrower has not entered into or granted any Security Agreements, or permitted the filing or attachment of any Security Interests on or affecting any of the Collateral directly or indirectly securing repayment of Borrower's Loan and Note, that would be prior or that may in any way be superior to Lender's Security Interests and rights in and to such Collateral.

Binding Effect. This Agreement, the Note, all Security Agreements (if any), and all Related Documents are binding upon the signers thereof, as well as upon their successors, representatives and assigns, and are legally enforceable in accordance with their respective terms.

AFFIRMATIVE COVENANTS. Borrower covenants and agrees with Lender that, so long as this Agreement remains in effect, Borrower will:

Notices of Claims and Litigation. Promptly inform Lender in writing of (1) all material adverse changes in Borrower's financial condition, and (2) all existing and all threatened litigation, claims, investigations, administrative proceedings or similar actions affecting Borrower or any Guarantor which could materially affect the financial condition of Borrower or the financial condition of any Guarantor.

Financial Records. Maintain its books and records in accordance with GAAP, applied on a consistent basis, and permit Lender to examine and audit Borrower's books and records at all reasonable times.

Financial Statements. Furnish Lender with the following:

Annual Statements. As soon as available, but in no event later than one-hundred-twenty (120) days after the end of each fiscal year, Borrower's balance sheet and income statement for the year ended, prepared by Borrower.

Interim Statements. As soon as available, but in no event later than sixty (60) days after the end of each of the first three fiscal quarters, Borrower's cumulative balance sheet and profit and loss statement for the period ended, prepared by Borrower.

Additional Requirements. Such other financial statements and related information in such form and detail as may be satisfactory to Lender within thirty (30) days of Lender's request. For the avoidance of doubt, Borrower agrees that all financial statements and other information required to be delivered to Lender under this Agreement or any Related Document will be delivered for the most recent fiscal or calendar period (as applicable) ended immediately prior to the date hereof and each fiscal or calendar period thereafter as required herein or in any Related Document.

All financial reports required to be provided under this Agreement shall be prepared in accordance with GAAP, applied on a consistent basis, and certified by Borrower as being true and correct.

Additional Information. Furnish such additional information and statements, as Lender may request from time to time.

Financial Covenants and Ratios. Comply with the following covenants and ratios:

Minimum Income and Cash flow Requirements. Borrower shall comply with the following cash flow ratio requirements:

Debt Service Coverage Ratio. Maintain a ratio of Debt Service Coverage equal to or in excess of 1.250 to 1.000. "Debt Service Coverage Ratio" means, on a consolidated basis with its consolidated subsidiaries and/or affiliates, or on a combined basis with its affiliates, EBITDA (earnings before interest expense, tax expense, depreciation expense and amortization expense) for the then current fiscal year of Borrower less the sum of cash taxes, cash dividends/distributions and un-financed capital expenditures, divided by the sum of current maturities of long-term debt and capital leases, and interest expense. This coverage ratio should be maintained at all times and may be evaluated at any time.

Tangible Net Worth Requirements. Borrower shall comply with the following net worth ratio requirements:

Total Unsubordinated Liabilities/Tangible Net Worth Ratio. Maintain a ratio of Total Unsubordinated Liabilities/Tangible Net Worth not in excess of 3.000 to 1.000. Total Unsubordinated Liabilities/Tangible Net Worth means, on a consolidated basis with its consolidated subsidiaries and/or affiliates, a ratio of Total Unsubordinated Liabilities divided by Tangible Net Worth. "Total Unsubordinated Liabilities" means total liabilities less any debt subordinated to Lender, and "Tangible Net Worth" means total assets less the sum of (1) total liabilities net of any debt subordinated to Lender, (2) net intangible assets, and (3) all amounts due from shareholders, officers, employees, and affiliates. This leverage ratio should be maintained at all times and may be evaluated at any time.

Except as provided above, all computations made to determine compliance with the requirements contained in this paragraph shall be made in accordance with generally accepted accounting principles, applied on a consistent basis, and certified by Borrower as being true and correct.

Insurance. Maintain fire and other risk insurance, public liability insurance, and such other insurance as Lender may require with respect to Borrower's properties and operations, in form, amounts, coverages and with insurance companies acceptable to Lender. Borrower, upon request of Lender, will deliver to Lender from time to time the policies or certificates of insurance in form satisfactory to Lender, including stipulations that coverages will not be cancelled or diminished without at least ten (10) days prior written notice to Lender. Each insurance policy also shall include an endorsement providing that coverage in favor of Lender will not be impaired in any way by any act, omission or default of Borrower or any other person. In connection with all policies covering assets in which Lender holds or is offered a security interest for the Loans, Borrower will provide Lender with such lender's loss payable or other endorsements as Lender may require.

Insurance Reports. Furnish to Lender, upon request of Lender, reports on each existing insurance policy showing such information as Lender may reasonably request, including without limitation the following: (1) the name of the insurer; (2) the risks insured; (3) the amount of the policy; (4) the properties insured; (5) the then current property values on the basis of which Insurance has been obtained, and the manner of determining those values; and (6) the expiration date of the policy.

Guaranties. Prior to disbursement of any Loan proceeds, furnish executed guaranties of the Loans in favor of Lender, executed by the guarantor named below, on Lender's forms, and in the amount and under the conditions set forth in those guaranties.

<u>Name of Guarantor</u>	<u>Amount</u>
Challenge/Surge Inc.	Unlimited

Other Agreements. Comply with all terms and conditions of all other agreements, whether now or hereafter existing, between Borrower and any other party and notify Lender immediately in writing of any default in connection with any other such agreements.

Loan Proceeds. Use all Loan proceeds solely for Borrower's business operations, unless specifically consented to the contrary by Lender in writing.

Taxes, Charges and Liens. Pay and discharge when due all of its indebtedness and obligations, including without limitation all assessments, taxes, governmental charges, levies and liens, of every kind and nature, Imposed upon Borrower or its properties, income, or profits, prior to the date on which penalties would attach, and all lawful claims that, if unpaid, might become a lien or charge upon any of Borrower's properties, income, or profits. Provided however, Borrower will not be required to pay and discharge any such assessment, tax, charge, levy, lien or claim so long as (1) the legality of the same shall be contested in good faith by appropriate proceedings, and (2) Borrower shall have established on Borrower's books adequate reserves with respect to such contested assessment, tax, charge, levy, lien, or claim in accordance with GAAP.

Performance. Perform and comply, in a timely manner, with all terms, conditions, and provisions set forth in this Agreement, in the Related Documents, and in all other instruments and agreements between Borrower and Lender. Borrower shall notify Lender immediately in writing of any default in connection with any agreement.

Operations. Maintain executive and management personnel with substantially the same qualifications and experience as the present executive and management personnel; provide written notice to Lender of any change in executive and management personnel; conduct its business affairs in a reasonable and prudent manner.

Environmental Studies. Promptly conduct and complete, at Borrower's expense, all such investigations, studies, samplings and testings as may be requested by Lender or any governmental authority relative to any substance, or any waste or by-product of any substance defined as toxic or a hazardous substance under applicable federal, state, or local law, rule, regulation, order or directive, at or affecting any property or any facility owned, leased or used by Borrower.

Compliance with Governmental Requirements. Comply with all laws, ordinances, and regulations, now or hereafter in effect, of all governmental authorities applicable to the conduct of Borrowers properties, businesses and operations, and to the use or occupancy of the Collateral, including without limitation, the Americans With Disabilities Act. Borrower may contest in good faith any such law, ordinance, or regulation and withhold compliance during any proceeding, including appropriate appeals, so long as Borrower has notified Lender in writing prior to doing so and so long as, in Lenders sole opinion, Lenders interests in the Collateral are not jeopardized. Lender may require Borrower to post adequate security or a surety bond, reasonably satisfactory to Lender, to protect Lenders interest.

Inspection. Permit employees or agents of Lender at any reasonable time to inspect any and all Collateral for the Loan or Loans and Borrowers other properties and to examine or audit Borrower's books, accounts, and records and to make copies and memoranda of Borrowers books, accounts, and records. If Borrower now or at any time hereafter maintains any records (Including without limitation computer generated records and computer software programs for the generation of such records) in the possession of a third party, Borrower, upon request of Lender, shall notify such party to permit Lender free access to such records at all reasonable times and to provide Lender with copies of any records it may request, all at Borrowers expense.

Environmental Compliance and Reports. Borrower shall comply in all respects with any and all Environmental Laws; not cause or permit to exist, as a result of an intentional or unintentional action or omission on Borrowers part or on the part of any third party, on property owned and/or occupied by Borrower, any environmental activity where damage may result to the environment, unless such environmental activity is pursuant to and in compliance with the conditions of a permit issued by the appropriate federal, state or local governmental authorities; shall furnish to Lender promptly and in any event within thirty (30) days after receipt thereof a copy of any notice, summons, lien, citation, directive, letter or other communication from any governmental agency or instrumentality concerning any intentional or unintentional action or omission on Borrowers part in connection with any environmental activity whether or not there is damage to the environment and/or other natural resources.

Additional Assurances. Make, execute and deliver to Lender such promissory notes, mortgages, deeds of trust, security agreements, assignments, financing statements, instruments, documents and other agreements as Lender or its attorneys may reasonably request to evidence and secure the Loans and to perfect all Security Interests.

Continuing Certification for Advances. By requesting an Advance, Borrower shall be deemed to have certified as of the date of the request, among other things, that all representations and warranties in this Agreement continue to be true and correct in all material respects, that no Event of Default exists under this Agreement or will result from the taking of the Advance, and that the Advance, when aggregated with all outstanding Advances hereunder, will not exceed the Borrowing Base.

Borrowing Base Certificate. For the purpose of determining availability of funds under the Note, Borrower agrees to provide to Lender as soon as available, but in any event within fifteen (15) days after the end of each calendar month, a Borrowing Base Certificate in form and substance satisfactory to Lender.

Insurance Requirements. For the avoidance of doubt regarding the requirement in this Agreement that Borrower maintain such insurance as Lender shall require, and except to the extent specific insurance types, coverages or insurers are specified in this Agreement or the Related Documents, Lender requires and Borrower agrees to maintain at all times with financially sound and reputable insurance companies such public liability insurance, property damage insurance and casualty insurance with respect to liabilities, losses or damage in respect of the assets and businesses of Borrower as may customarily be carried or maintained under similar circumstances by businesses engaged in the same or similar enterprises, in each case in such amounts, with such deductibles, covering such risks and otherwise on terms and conditions as shall be customary for such businesses.

Eligible Accounts Aging. Within fifteen (15) days after the end of each month, furnish to Lender an Eligible Accounts (receivables or payables) Aging Report, of Borrower, Challenge/Surge Inc. and Surge Components Limited, in form and substance satisfactory to Lender and in any event to include the number of days each such Account has been outstanding and the payment terms of the Accounts as of the last day of each month, together with a reconciliation with Borrowers general ledger or interim financial statement.

Eligible Inventory Aging. Within fifteen (15) days after the end of each month, furnish to Lender an Eligible Inventory listing, in form and substance satisfactory to Lender of Borrower, Challenge/Surge Inc. and Surge Components Limited in form and substance satisfactory to Lender and in any event to include the location and status of the Inventory.

RECOVERY OF ADDITIONAL COSTS. If the imposition of or any change in any law, rule, regulation, guideline, or generally accepted accounting principle, or the interpretation or application of any thereof by any court, administrative or governmental authority, or standard-setting organization (including any request or policy not having the force of law) shall impose, modify or make applicable any taxes (except federal, state or local income or franchise taxes Imposed on Lender), reserve requirements, capital adequacy requirements or other obligations which would (A) increase the cost to Lender for extending or maintaining the credit facilities to which this Agreement relates, (B) reduce the amounts payable to Lender under this Agreement or the Related Documents, or (C) reduce the rate of return on Lender's capital as a consequence of Lenders obligations with respect to the credit facilities to which this Agreement relates, then Borrower agrees to pay Lender such additional amounts as will compensate Lender therefor, within five (5) days after Lenders written demand for such payment, which demand shall be accompanied by an explanation of such imposition or charge and a calculation in reasonable detail of the additional amounts payable by Borrower, which explanation and calculations shall be conclusive in the absence of manifest error.

LENDER'S EXPENDITURES. If any action or proceeding is commenced that would materially affect Lenders interest in the Collateral or if Borrower fails to comply with any provision of this Agreement or any Related Documents, including but not limited to Borrower's failure to discharge or pay when due any amounts Borrower is required to discharge or pay under this Agreement or any Related Documents, Lender on Borrowers behalf may (but shall not be obligated to) take any action that Lender deems appropriate, including but not limited to discharging or paying all taxes, liens, security interests, encumbrances and other claims, at any lime levied or placed on any Collateral and paying all costs for insuring, maintaining and preserving any Collateral. All such expenditures incurred or paid by Lender for such purposes, with the exception of insurance premiums paid by Lender with respect to motor vehicles, but including the payment of attorneys' fees and expenses, will then bear interest at the rate charged under the Note from the date incurred or paid by Lender to the date of repayment by Borrower. All such expenses will become a part of the Indebtedness and, at Lender's option, will (A) be payable on demand; (B) be added to the balance of the Note and be apportioned among and be payable with any installment payments to become due during either (1) the term of any applicable insurance policy; or (2) the remaining term of the Note; or (C) be treated as a balloon payment which will be due and payable at the Note's maturity.

NEGATIVE COVENANTS. Borrower covenants and agrees with Lender that while this Agreement is in effect, Borrower shall not, without the prior written consent of Lender,

Indebtedness and Liens. (1) Except for trade debt incurred in the normal course of business and indebtedness to Lender contemplated by this Agreement, create, incur or assume indebtedness for borrowed money, including capital leases, (2) sell, transfer, mortgage, assign, pledge, lease, grant a security interest in, or encumber any of Borrower's assets (except as allowed as Permitted Liens), or (3) sell with recourse any of Borrower's accounts, except to Lender.

Continuity of Operations. (1) Engage in any business activities substantially different than those in which Borrower is presently engaged, (2) cease operations, liquidate, merge, transfer, acquire or consolidate with any other entity, change its name, dissolve or transfer or sell Collateral out of the ordinary course of business, or (3) pay any dividends on Borrower's stock (other than dividends payable in its stock), provided, however that notwithstanding the foregoing, but only so long as no Event of Default has occurred and is continuing or would result from the payment of dividends, if Borrower is a "Subchapter S Corporation" (as defined in the Internal Revenue Code of 1986, as amended), Borrower may pay cash dividends on its stock to its shareholders from time to time in amounts necessary to enable the shareholders to pay income taxes and make estimated income tax payments to satisfy their liabilities under federal and state law which arise solely from their status as Shareholders of a Subchapter S Corporation because of their ownership of shares of Borrower's stock, or purchase or retire any of Borrower's outstanding shares or alter or amend Borrower's capital structure.

Loans, Acquisitions and Guaranties. (1) Loan, invest in or advance money or assets to any other person, enterprise or entity, (2) purchase, create or acquire any interest in any other enterprise or entity, or (3) incur any obligation as surety or guarantor other than in the ordinary course of business.

Agreements. Enter into any agreement containing any provisions which would be violated or breached by the performance of Borrower's obligations under this Agreement or in connection herewith.

CESSATION OF ADVANCES. If Lender has made any commitment to make any Loan to Borrower, whether under this Agreement or under any other agreement, Lender shall have no obligation to make Loan Advances or to disburse Loan proceeds if: (A) Borrower or any Guarantor is in default under the terms of this Agreement or any of the Related Documents or any other agreement that Borrower or any Guarantor has with Lender, (B) Borrower or any Guarantor dies, becomes incompetent or becomes insolvent, files a petition in bankruptcy or similar proceedings, or is adjudged a bankrupt; (C) there occurs a material adverse change in Borrower's financial condition, in the financial condition of any Guarantor, or in the value of any Collateral securing any Loan; or (D) any Guarantor seeks, claims or otherwise attempts to limit, modify or revoke such Guarantor's guaranty of the Loan or any other loan with Lender; or (E) Lender in good faith deems itself insecure, even though no Event of Default shall have occurred.

RIGHT OF SETOFF. To the extent permitted by applicable law, Lender reserves a right of setoff in all Borrower's accounts with Lender and its subsidiaries and affiliates (whether checking, savings, or some other account and whether evidenced by a certificate of deposit). This includes all accounts Borrower holds jointly with someone else and all accounts Borrower may open in the future. However, this does not include any IRA or Keogh accounts, or any trust accounts for which setoff would be prohibited by law. Borrower authorizes Lender, to the extent permitted by applicable law, to charge or setoff all sums owing on the Indebtedness against any and all such accounts, and, at Lender's option, to administratively freeze all such accounts to allow Lender to protect Lender's charge and setoff rights provided in this paragraph.

DEFAULT. Default will occur if payment of the Indebtedness in full is not made immediately when due.

EFFECT OF AN EVENT OF DEFAULT. If any Event of Default shall occur, except where otherwise provided in this Agreement or the Related Documents, any commitments and obligations of Lender under this Agreement or the Related Documents or any other agreement immediately will terminate (including any obligation to make further Loan Advances or disbursements), and, at Lender's option, all Indebtedness immediately will become due and payable, all without notice of any kind to Borrower, except that in the case of an Event of Default of the type described in the "Insolvency" subsection above, such acceleration shall be automatic and not optional. In addition, Lender shall have all the rights and remedies provided in the Related Documents or available at law, in equity, or otherwise. Except as may be prohibited by applicable law, all of Lender's rights and remedies shall be cumulative and may be exercised singularly or concurrently. Election by Lender to pursue any remedy shall not exclude pursuit of any other remedy, and an election to make expenditures or to take action to perform an obligation of Borrower or of any Grantor shall not affect Lender's right to declare a default and to exercise its rights and remedies.

PRIMARY DEMAND DEPOSIT ACCOUNT. Until such time as all of Borrower's Loans have been paid in full and this Agreement has been terminated, Borrower agrees to maintain its Primary Demand Deposit Account with Lender. "Primary Demand Deposit Account" means the business demand deposit account into which substantially all of Borrower's receipts from its operations are deposited and from which substantially all of Borrower's disbursements for its operations are made. During any period of time Borrower fails to maintain its Primary Demand Deposit Account with Lender, the rate of interest payable under the Note executed by Borrower in connection with this Agreement shall be increased by one percent (1%) per annum. Borrower authorizes Lender to automatically deduct all payments required to be made by this Agreement from Borrower's Primary Demand Deposit Account.

UNCOMMITTED LOANS. Notwithstanding anything to the contrary herein or elsewhere, Borrower acknowledges and agrees that, (i) each Loan is uncommitted, (ii) Lender may refuse, at its sole and absolute discretion, to make an Advance without prior notice to Borrower and (iii) Borrower's performance or compliance with the terms of this Agreement or any Related Document shall not obligate Lender to make an Advance or provide any other extension of credit.

JURY WAIVER. BORROWER HEREBY WAIVES THE RIGHT TO A TRIAL BY JURY IN ANY ACTION, PROCEEDING, OR COUNTERCLAIM ARISING HEREUNDER OR IN CONNECTION HERewith TO THE EXTENT PERMITTED BY APPLICABLE LAW.

MISCELLANEOUS PROVISIONS. The following miscellaneous provisions are a part of this Agreement:

Amendments. This Agreement, together with any Related Documents, constitutes the entire understanding and agreement of the parties as to the matters set forth in this Agreement. No alteration of or amendment to this Agreement shall be effective unless given in writing and signed by the party or parties sought to be charged or bound by the alteration or amendment.

Attorneys' Fees; Expenses. Borrower agrees to pay upon demand all of Lender's costs and expenses, including Lender's reasonable attorneys' fees and Lender's legal expenses, Incurred in connection with the enforcement of this Agreement. Lender may hire or pay someone else to help enforce this Agreement, and Borrower shall pay the costs and expenses of such enforcement. Costs and expenses include Lenders reasonable attorneys' fees and legal expenses whether or not there is a lawsuit, including reasonable attorneys' fees and legal expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Borrower also shall pay all court costs and such additional fees as may be directed by the court.

Caption Headings. Caption headings in this Agreement are for convenience purposes only and are not to be used to Interpret or define the provisions of this Agreement.

Consent to Loan Participation. Borrower agrees and consents to Lender's sale or transfer, whether now or later, of one or more participation interests in the Loan to one or more purchasers, whether related or unrelated to Lender. Lender may provide, without any limitation whatsoever, to any one or more purchasers, or potential purchasers, any information or knowledge Lender may have about Borrower or about any other matter relating to the Loan, and Borrower hereby waives any rights to privacy Borrower may have with respect to such matters. Borrower additionally waives any and all notices of sale of participation interests, as well as all notices of any repurchase of such participation interests. Borrower also agrees that the purchasers of any such participation interests will be considered as the absolute owners of such interests in the Loan and will have all the rights granted under the participation agreement or agreements governing the sale of such participation interests. Borrower further waives all rights of offset or counterclaim that it may have now or later against Lender or against any purchaser of such a participation interest and unconditionally agrees that either Lender or such purchaser may enforce Borrower's obligation under the Loan irrespective of the failure or insolvency of any holder of any interest in the Loan. Borrower further agrees that the purchaser of any such participation interests may enforce its Interests irrespective of any personal claims or defenses that Borrower may have against Lender.

Governing Law. This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of New York without regard to its conflicts of law provisions.

Choice of Venue. If there is a lawsuit, Borrower agrees upon Lender's request to submit to the jurisdiction of the courts of New York County, State of New York. Nothing herein shall affect the right of the Lender to bring any action or proceeding against the Borrower or its property in the courts of any other jurisdiction.

No Waiver by Lender. Lender shall not be deemed to have waived any rights under this Agreement unless such waiver is given in writing and signed by Lender. No delay or omission on the part of Lender in exercising any right shall operate as a waiver of such right or any other right. A waiver by Lender of a provision of this Agreement shall not prejudice or constitute a waiver of Lender's right otherwise to demand strict compliance with that provision or any other provision of this Agreement. No prior waiver by Lender, nor any course of dealing between Lender and Borrower, or between Lender and any Grantor, shall constitute a waiver of any of Lender's rights or of any of Borrower's or any Grantor's obligations as to any future transactions. Whenever the consent of Lender is required under this Agreement, the granting of such consent by Lender in any instance shall not constitute continuing consent to subsequent instances where such consent is required and in all cases such consent may be granted or withheld in the sole discretion of Lender.

Notices. Any notice required to be given under this Agreement shall be given in writing, and shall be effective when actually delivered, when actually received by telefacsimile (unless otherwise required by law), when deposited with a nationally recognized overnight courier, or, if mailed, when deposited in the United States mail, as first class, certified or registered mail postage prepaid, directed to the addresses shown near the beginning of this Agreement. Any party may change its address for notices under this Agreement by giving formal written notice to the other parties, specifying that the purpose of the notice is to change the party's address. For notice purposes, Borrower agrees to keep Lender Informed at all times of Borrower's current address. Unless otherwise provided or required by law, if there is more than one Borrower, any notice given by Lender to any Borrower is deemed to be notice given to all Borrowers.

Severability. If a court of competent jurisdiction finds any provision of this Agreement to be illegal, invalid, or unenforceable as to any circumstance, that finding shall not make the offending provision illegal, invalid, or unenforceable as to any other circumstance. If feasible, the offending provision shall be considered modified so that it becomes legal, valid and enforceable. If the offending provision cannot be so modified, it shall be considered deleted from this Agreement. Unless otherwise required by law, the illegality, invalidity, or unenforceability of any provision of this Agreement shall not affect the legality, validity or enforceability of any other provision of this Agreement.

Subsidiaries and Affiliates of Borrower. To the extent the context of any provisions of this Agreement makes it appropriate, including without limitation any representation, warranty or covenant, the word "Borrower" as used in this Agreement shall include all of Borrower's subsidiaries and affiliates. Notwithstanding the foregoing however, under no circumstances shall this Agreement be construed to require Lender to make any Loan or other financial accommodation to any of Borrower's subsidiaries or affiliates.

Successors and Assigns. All covenants and agreements by or on behalf of Borrower contained in this Agreement or any Related Documents shall bind Borrower's successors and assigns and shall inure to the benefit of Lender and its successors and assigns. Borrower shall not, however, have the right to assign Borrower's rights under this Agreement or any Interest therein, without the prior written consent of Lender.

Survival of Representations and Warranties. Borrower understands and agrees that in extending Loan Advances, Lender is relying on all representations, warranties, and covenants made by Borrower in this Agreement or in any certificate or other instrument delivered by Borrower to Lender under this Agreement or the Related Documents. Borrower further agrees that regardless of any investigation made by Lender, all such representations, warranties and covenants will survive the extension of Loan Advances and delivery to Lender of the Related Documents, shall be continuing in nature, shall be deemed made and redated by Borrower at the time each Loan Advance is made, and shall remain in full force and effect until such time as Borrower's Indebtedness shall be paid in full, or until this Agreement shall be terminated in the manner provided above, whichever is the last to occur.

Time is of the Essence. Time is of the essence in the performance of this Agreement.

DEFINITIONS. The following capitalized words and terms shall have the following meanings when used in this Agreement. Unless specifically stated to the contrary, all references to dollar amounts shall mean amounts in lawful money of the United States of America. Words and terms used in the singular shall include the plural, and the plural shall include the singular, as the context may require. Words and terms not otherwise defined in this Agreement shall have the meanings attributed to such terms in the Uniform Commercial Code. Accounting words and terms not otherwise defined in this Agreement shall have the meanings assigned to them in accordance with generally accepted accounting principles as in effect on the date of this Agreement:

Account. The word "Account" means a trade account, account receivable, other receivable, or other right to payment for goods sold or services rendered owing to Borrower (or to a third party grantor acceptable to Lender and, solely for reporting purposes, to Surge Components, Limited).

Account Debtor. The words "Account Debtor" mean the person or entity obligated upon an Account.

Advance. The word "Advance" means a disbursement of Loan funds made, or to be made, to Borrower or on Borrower's behalf under the terms and conditions of this Agreement.

Agreement. The word "Agreement" means this Business Loan Agreement (Asset Based), as this Business Loan Agreement (Asset Based) may be amended or modified from time to time, together with all exhibits and schedules attached to this Business Loan Agreement (Asset Based) from time to time.

Borrower. The word "Borrower" means Surge Components, Inc. and includes all co-signers and co-makers signing the Note and all their successors and assigns.

Borrowing Base. The words "Borrowing Base" mean, as determined by Lender from time to time, the lesser of (1) **\$3,000,000.00** or (2) the sum of (a) **80.000%** of the aggregate amount of Eligible Accounts of Borrower and Guarantor (not to exceed in corresponding Loan amount based on Eligible Accounts **\$3,000,000.00**), plus (b) **30.000%** of the aggregate amount of Eligible Inventory of Borrower and Guarantor (not to exceed in corresponding Loan amount based on Eligible Inventory **\$1,000,000.00**). **In no event shall Eligible Accounts and Eligible Inventory of Surge Components Limited, which must be provided for reporting purposes, be included in the Borrowing Base.**

Business Day. The words "Business Day" mean a day on which commercial banks are open in the State of New York.

Collateral. The word “Collateral” means all property and assets granted as collateral security for a Loan, whether real or personal property, whether granted directly or indirectly, whether granted now or in the future, and whether granted in the form of a security interest, mortgage, collateral mortgage, deed of trust, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factor’s lien, equipment trust, conditional sale, trust receipt, lien, charge, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever, whether created by law, contract, or otherwise. The word Collateral also includes without limitation all collateral described in the Collateral section of this Agreement.

Default. The word “Default” means the Default set forth in this Agreement in the section titled “Default”.

Eligible Accounts. The words “Eligible Accounts” mean at any time, all of Borrower’s Accounts and Guarantor’s Accounts which contain selling terms and conditions acceptable to Lender and *solely for reporting purposes*, the Accounts of Surge Component Limited. The net amount of any Eligible Account against which Borrower may borrow shall exclude all returns, discounts, credits, and offsets of any nature. Unless otherwise agreed to by Lender in writing, Eligible Accounts do not include:

- (1) Accounts with respect to which the Account Debtor is employee or agent of Borrower or Guarantor.
- (2) Accounts with respect to which the Account Debtor is a subsidiary of, or affiliated with Borrower or Guarantor or their respective shareholders, officers, or directors.
- (3) Accounts with respect to which goods are placed on consignment, guaranteed sale, or other terms by reason of which the payment by the Account Debtor may be conditional.
- (4) Accounts with respect to which Borrower or Guarantor is or may become liable to the Account Debtor for goods sold or services rendered by the Account Debtor to Borrower or Guarantor, as applicable.
- (5) Accounts which are subject to dispute, counterclaim, or setoff.
- (6) Accounts with respect to which the goods have not been shipped or delivered, or the services have not been rendered, to the Account Debtor.
- (7) Accounts with respect to which Lender, in its sole discretion, deems the creditworthiness or financial condition of the Account Debtor to be unsatisfactory.
- (8) Accounts of any Account Debtor who has filed or has had filed against it a petition in bankruptcy or an application for relief under any provision of any state or federal bankruptcy, Insolvency, or debtor-In-relief acts; or who has had appointed a trustee, custodian, or receiver for the assets of such Account Debtor, or who has made an assignment for the benefit of creditors or has become insolvent or fails generally to pay Its debts (including its payrolls) as such debts become due.
- (9) Accounts which have not been paid in full within ninety (90) days from the invoice date. The entire balance of any Account of any single Account Debtor will be ineligible whenever the portion of the Account which has not been paid within ninety (90) days from the invoice date is in excess of 25.000% of the total amount outstanding on the Account.
- (10) That portion of the Accounts of any single Account Debtor which exceeds **25.000%** of all of Borrower’s Accounts and Guarantor’s Accounts, determined both on an individual and combined basis.
- (11) Accounts which have not been billed or which are subject to retainage or holdbacks by the Account Debtor.
- (12) All Account Debtor deposits and all deferred revenue associated with any Account.

Eligible Inventory. The words “Eligible Inventory” mean, at any time, all of Borrower’s Inventory and Guarantor’s Inventory as defined below and *solely for reporting purposes*, the inventory of Surge Component Limited, except:

- (1) Inventory which is not owned by Borrower or Guarantor free and clear of all security interests, liens, encumbrances, and claims of third parties.
- (2) Inventory which Lender, in its sole discretion, deems to be obsolete, unsalable, damaged, defective, or unfit for further processing.
- (3) Inventory located outside the United States or in transit.
- (4) Inventory held in a warehouse that is not subject to a landlord waiver acceptable to Lender.
- (5) All Account Debtor deposits and all deferred revenue associated with any Inventory.

Environmental Laws. The words “Environmental Laws” mean any and all state, federal and local statutes, regulations and ordinances relating to the protection of human health or the environment, including without limitation the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, 42 U.S.C. Section 9601, et seq. (“CERCLA”), the Superfund Amendments and Reauthorization Act of 1986, Pub. L No. 99-499 (“SARA”), the Hazardous Materials Transportation Act, 49 U.S.C. Section 1801, et seq., the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901, et seq., or other applicable state or federal laws, rules, or regulations adopted pursuant thereto.

Event of Default. The words “Event of Default” mean any of the events of default set forth in this Agreement in the default section of this Agreement.

Expiration Date. The words “Expiration Date” mean the date of termination of Lender’s commitment to lend under this Agreement. GAAP. The word “GAAP” means generally accepted accounting principles.

Grantor. The word “Grantor” means each and all of the persons or entities granting a Security interest in any Collateral for the Loan, including without limitation all Borrowers and Guarantors granting such a Security Interest.

Guarantor. The word “Guarantor” means any guarantor, surety, or accommodation party of any or all of the Loan.

Hazardous Substances. The words “Hazardous Substances” mean materials that, because of their quantity, concentration or physical, chemical or infectious characteristics, may cause or pose a present or potential hazard to human health or the environment when improperly used, treated, stored, disposed of, generated, manufactured, transported or otherwise handled. The words “Hazardous Substances” are used in their very broadest sense and include without limitation any and all hazardous or toxic substances, materials or waste as defined by or listed under the Environmental Laws. The term “Hazardous Substances” also includes, without limitation, petroleum and petroleum by-products or any fraction thereof and asbestos.

Indebtedness. The word “Indebtedness” means all present and future loans, advances, overdrafts, liabilities, obligations, guaranties, covenants, duties and other debts at any time owing by Borrower to Lender, whether evidenced by this Agreement, a promissory note or other instrument, any Related Documents, or any other document or agreement, whether arising from an extension of credit, opening of a letter of credit, banker’s acceptance, loan, overdraft, guaranty, indemnification or otherwise, whether direct or indirect (including, without limitation, those acquired by assignment and any participation by Lender in Borrower’s debts owing to others), absolute or contingent, due or to become due, including, without limitation, all interest, charges, expenses, fees, attorneys’ fees (including attorneys’ fees and expenses incurred in bankruptcy), expert witness fees and expenses, fees and expenses of consultants, audit fees, letter of credit fees, dosing fees, facility fees, termination fees, and any other sums chargeable to Borrower under this Agreement, the Note, any Related Documents, or under any other present or future instrument, document or agreement between Borrower and Lender.

Inventory. The word “Inventory” means all raw materials, work in process, finished goods, merchandise, parts and supplies, of every kind and description, and goods held for sale or lease or furnished under contracts of service of Borrower (or that of a third party Grantor acceptable to Lender and solely for reporting purposes, that of Surge Components, Limited) in which Borrower (or such third party Grantor or Surge Components Limited) now has or hereafter acquires any right, whether held by Borrower or others, and all documents of title, warehouse receipts, bills of lading, and all other documents of every type covering all or any part of the foregoing. Inventory includes inventory temporarily out of Borrower’s (or such third party Grantor’s or solely for reporting purposes, that of Surge Components Limited’s) custody or possession and all returns on Accounts.

Lender. The word “Lender” means Citibank, N.A., its successors and assigns.

Loan. The word “Loan” means any and all loans and financial accommodations from Lender to Borrower whether now or hereafter existing, and however evidenced, including without limitation those loans and financial accommodations described herein or described on any exhibit or schedule attached to this Agreement from time to time.

Note. The word “Note” means and includes without limitation Borrower’s promissory note or notes, if any, or any credit agreements or loan agreements, evidencing Borrower’s Indebtedness, as well as any substitute, replacement or refinancing note or notes or credit agreement or loan agreement therefor.

Permitted Liens. The words “Permitted Liens” mean (1) liens and security interests securing Indebtedness owed by Borrower to Lender, (2) liens for taxes, assessments, or similar charges either not yet due or being contested in good faith; (3) liens of materialmen, mechanics, warehousemen, or carriers, or other like liens arising in the ordinary course of business and securing obligations which are not yet delinquent; (4) purchase money liens or purchase money security interests upon or in any property acquired or held by Borrower in the ordinary course of business to secure indebtedness outstanding on the date of this Agreement or permitted to be incurred under the paragraph of this Agreement titled “Indebtedness and Liens”; (5) liens and security interests which, as of the date of this Agreement, have been disclosed to and approved by the Lender in writing; and (6) those liens and security interests which in the aggregate constitute an immaterial and insignificant monetary amount with respect to the net value of Borrower’s assets.

Primary Credit Facility. The words “Primary Credit Facility” mean the credit facility described in the Line of Credit section of this Agreement.

Related Documents. The words “Related Documents” mean all promissory notes, credit agreements, loan agreements, environmental agreements, guaranties, security agreements, mortgages, deeds of trust, security deeds, collateral mortgages, and all other instruments, agreements and documents, whether now or hereafter existing, executed in connection with the Loan.

Security Agreement. The words "Security Agreement" mean and include without limitation any agreements, promises, covenants, arrangements, understandings or other agreements, whether created by law, contract, or otherwise, evidencing, governing, representing, or creating a Security Interest.

Security Interest. The words "Security Interest" mean, without limitation, any and all types of collateral security, present and future, whether in the form of a lien, charge, encumbrance, mortgage, deed of trust, security deed, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factors lien, equipment trust, conditional sale, trust receipt, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever whether created by law, contract, or otherwise.

BORROWER ACKNOWLEDGES HAVING READ ALL THE PROVISIONS OF THIS BUSINESS LOAN AGREEMENT (ASSET BASED) AND BORROWER AGREES TO ITS TERMS. THIS BUSINESS LOAN AGREEMENT (ASSET BASED) IS DATED FEBRUARY 22, 2017.

BORROWER:

SURGE COMPONENTS, INC.

By: /s/ Ira Levy
Ira Levy, Chief Executive Officer of Surge Components, Inc.

By: /s/ Steven Lubman
Steven Lubman, President of Surge Components, Inc.

LENDER:

CITIBANK, N.A.


By: 
Authorized Signer

Exhibit 10.2



PROMISSORY NOTE

Borrower: Surge Components, Inc.
95 East Jefryn Boulevard
Deer Park, NY 11729

Lender: Citibank, N.A.
6801 Colwell Boulevard
Irving, TX 75039

Principal Amount: \$3,000,000.00

Date of Note: February 22, 2017

PROMISE TO PAY. To repay Borrower's loan, Surge Components, Inc. ("Borrower") promises to pay to Citibank, N.A. ("Lender"), or order, in lawful money of the United States of America, on demand, the principal amount of Three Million & 00/100 Dollars (\$3,000,000.00) or so much as may be outstanding, together with interest on the unpaid outstanding principal balance calculated from the date of the first advance until repayment of all advances.

PAYMENT. Borrower will pay this loan in full immediately upon Lender's demand. Borrower will pay regular monthly payments of all accrued unpaid interest due as of each payment date, beginning March 22, 2017, with all subsequent interest payments to be due on the same day of each month after that. Unless otherwise agreed or required by applicable law, payments will be applied to the loan in the following order: (1) interest; (2) principal; and (3) charges, fees and penalties. Borrower will pay Lender at Lender's address shown above or at such other place as Lender may designate in writing.

ADVANCES. Borrower understands and agrees that all advances under this Note are at Lender's sole and absolute discretion and Lender, without notice to the Borrower, may decline to make any advance requested by Borrower, regardless of the manner in which the request is made.

VARIABLE INTEREST RATE. The interest rate on this Note is subject to change from time to time based on changes in an independent index which is the greater of the Prime Rate or the Minimum Interest Rate, each as hereafter defined (the "Index"). The Index is not necessarily the lowest rate charged by Lender on its loans. If the Index becomes unavailable during the term of this loan, Lender may designate a substitute index after notifying Borrower. Lender will tell Borrower the current Index rate upon Borrower's request. The interest rate change will not occur more often than each day the Index changes. Borrower understands that Lender may make loans based on other rates as well. Interest on the unpaid principal balance of this Note will be calculated as described in the "INTEREST CALCULATION METHOD" paragraph using a rate equal to the Index. NOTICE: Under no circumstances will the interest rate on this Note be more than the maximum rate allowed by applicable law.

INTEREST CALCULATION METHOD. Interest on this Note is computed on a 365360 basis; that is, by applying the ratio of the interest rate over a year of 360 days, multiplied by the outstanding principal balance, multiplied by the actual number of days the principal balance is outstanding. All interest payable under this Note is computed using this method.

PRIME RATE. "Prime Rate" shall mean the prime rate of interest announced by Lender from time to time at its principal office as its prime commercial lending rate.

MINIMUM INTEREST RATE. "Minimum Interest Rate" shall mean two hundred (200) basis points in excess of the rate of Interest determined by Lender in accordance with its customary procedures and utilizing such electronic or other quotation sources as it considers appropriate to be the prevailing rate per annum in effect each banking day at which deposits in United States dollars for a one month period, determined by Lender in its sole discretion, are offered to Lender by first class banks in the London Interbank Market shortly after 11:00 a.m. (London time) two banking days prior to the date such rate of interest shall be effective and applied to existing and future advances with respect to this Note.

PREPAYMENT. Borrower may pay without fee all or a portion of the amount owed earlier than it is due. Early payments will not, unless agreed to by Lender in writing, relieve Borrower of Borrower's obligation to continue to make payments of accrued unpaid interest. Rather, early payments will reduce the principal balance due. Borrower agrees not to send Lender payments marked "paid in full", "without recourse", or similar language. If Borrower sends such a payment, Lender may accept it without losing any of Lender's rights under this Note, and Borrower will remain obligated to pay any further amount owed to Lender. **All written communications concerning disputed amounts, including any check or other payment instrument that indicates that the payment constitutes "payment in full" of the amount owed or that is tendered with other conditions or limitations or as full satisfaction of a disputed amount must be mailed or delivered to: Citibank, N.A.; 6801 Colwell Boulevard; Irving, TX 75039.**

INTEREST AFTER DEFAULT - RELATED DOCUMENTS. Upon the failure by Borrower to repay all amounts due under this Note upon Lender's demand or observe or comply with any of the terms or conditions herein or in any Related Documents, Lender, at its option, may, if permitted under applicable law, increase the Interest rate on this Note by 3.00%. The interest rate will not exceed the maximum rate permitted by applicable law. The words "Related Documents" mean all promissory notes, credit agreements, loan agreements, environmental agreements, guaranties, security agreements, mortgages, deeds of trust, security deeds, collateral mortgages, and all other instruments, agreements and documents, whether now or hereafter existing, executed in connection with any and all loans and financial accommodations from Lender to Borrower whether now or hereafter existing, and however evidenced, including without limitation those loans and financial accommodations described herein or described on any exhibit or schedule attached to this Agreement from time to time. This section replaces and supersedes the section below entitled "Interest After Default," which shall be disregarded and have no force or effect.

PROMISSORY NOTE
(Continued)

Page 2

LATE CHARGE. If a regularly scheduled interest payment is 15 days or more late, Borrower will be charged 4.000% of the unpaid portion of the regularly scheduled payment. If Lender demands payment of this loan, and Borrower does not pay the loan in full within 15 days after Lender's demand, Borrower also will be charged 4.000% of the unpaid portion of the sum of the unpaid principal plus accrued unpaid interest.

INTEREST AFTER DEFAULT. Upon the failure of the Borrower to pay any amount hereunder on demand, Lender, at its option, may, if permitted under applicable law, increase the interest rate on this Note to 3.000 percentage points above the index. The interest rate will not exceed the maximum rate permitted by applicable law.

LENDER'S RIGHTS. Upon the failure of the borrower to pay any amount hereunder on demand, Lender may declare the entire unpaid principal balance on this Note and all accrued unpaid interest immediately due and payable.

ATTORNEYS' FEES; EXPENSES. Borrower agrees to pay all costs and expenses Lender incurs to collect this Note. This includes, subject to any limits under applicable law, Lenders reasonable attorneys' fees and Lender's legal expenses whether or not there is a lawsuit, including reasonable attorneys' fees and expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), and appeals. If not prohibited by applicable law, Borrower also will pay any court costs, in addition to all other sums provided by law.

GOVERNING LAW. This Note will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of New York without regard to Its conflicts of law provisions.

CHOICE OF VENUE. If there is a lawsuit, Borrower agrees upon Lender's request to submit to the jurisdiction of the courts of New York County, State of New York. Nothing herein shall affect the right of the Lender to bring any action or proceeding against the Borrower or its property in the courts of any other jurisdiction.

RIGHT OF SETOFF. To the extent permitted by applicable law, Lender reserves a right of setoff in all Borrowers accounts with Lender and its subsidiaries and affiliates (whether checking, savings, or some other account and whether evidenced by a certificate of deposit). This includes all accounts Borrower holds jointly with someone else and all accounts Borrower may open in the future. However, this does not include any IRA or Keogh accounts, or any trust accounts for which setoff would be prohibited by law. Borrower authorizes Lender, to the extent permitted by applicable law, to charge or setoff all sums owing on the indebtedness against any and all such accounts, and, at Lender's option, to administratively freeze all such accounts to allow Lender to protect Lender's charge and setoff rights provided in this paragraph.

LINE OF CREDIT. This Note evidences a revolving line of credit. Advances under this Note, as well as directions for payment from Borrower's accounts, may be requested orally or in writing by Borrower or by an authorized person. Lender may, but need not, require that all oral requests be confirmed in writing. Borrower agrees to be liable for all sums either: (A) advanced in accordance with the instructions of an authorized person or (B) credited to any of Borrower's accounts with Lender. The unpaid principal balance owing on this Note at any time may be evidenced by endorsements on this Note or by Lender's internal records, including daily computer print-outs. Lender will have no obligation to advance funds under this Note if: (A) Borrower or any guarantor is in default under the terms of this Note or any agreement that Borrower or any guarantor has with Lender, including any agreement made in connection with the signing of this Note; (B) Borrower or any guarantor ceases doing business or is insolvent; (C) any guarantor seeks, claims or otherwise attempts to limit, modify or revoke such guarantor's guarantee of this Note or any other loan with Lender; (D) Borrower has applied funds provided pursuant to this Note for purposes other than those authorized by Lender; or (E) Lender in good faith believes itself insecure.

PROMISSORY NOTE
(Continued)

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LINE OF CREDIT - ONLINE ACCESS. Requests for advances under this Note to bear interest at the Prime Rate or the Minimum Interest Rate, as well as payments from Borrower's accounts, may also be made on Lender's online banking system. Borrower agrees to be liable for all sums either (A) advanced in accordance with the online instructions or (B) credited to any of Borrower's accounts with Lender.

JURY WAIVER. BORROWER HEREBY WAIVES THE RIGHT TO A TRIAL BY JURY IN ANY ACTION, PROCEEDING, OR COUNTERCLAIM ARISING HEREUNDER OR IN CONNECTION HERewith TO THE EXTENT PERMITTED BY APPLICABLE LAW.

SUCCESSOR INTERESTS. The terms of this Note shall be binding upon Borrower, and upon Borrower's heirs, personal representatives, successors and assigns, and shall inure to the benefit of Lender and its successors and assigns.

GENERAL PROVISIONS. This Note is payable on demand. The inclusion of specific default provisions or rights of Lender shall not preclude Lender's right to declare payment of this Note on its demand. If any part of this Note cannot be enforced, this fact will not affect the rest of the Note. Lender may delay or forgo enforcing any of its rights or remedies under this Note without losing them. Borrower and any other person who signs, guarantees or endorses this Note, to the extent allowed by law, waive presentment, demand for payment, and notice of dishonor. Upon any change in the terms of this Note, and unless otherwise expressly stated in writing, no party who signs this Note, whether as maker, guarantor, accommodation maker or endorser, shall be released from liability. All such parties agree that Lender may renew or extend (repeatedly and for any length of time) this loan or release any party or guarantor or collateral; or impair, fail to realize upon or perfect Lender's security interest in the collateral; and take any other action deemed necessary by Lender without the consent of or notice to anyone. All such parties also agree that Lender may modify this loan without the consent of or notice to anyone other than the party with whom the modification is made. The obligations under this Note are joint and several.

BORROWER:

SURGE COMPONENTS, INC.

By: /s/ Ira Levy
Ira Levy, President/Chief Executive Officer of Surge
Components, Inc.

By: /s/ Steven Lubman
Steven Lubman, Vice President of Surge Components, Inc.

EXHIBIT 31.1

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
AND PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002**

I, Ira Levy, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Surge Components, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: April 14, 2017

By: /s/ Ira Levy

Ira Levy
Chief Executive Officer
(Principal Executive Officer and
Principal Financial Officer)

EXHIBIT 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Surge Components, Inc. (the "Company") on Form 10-Q for the period ended February 28, 2017 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ira Levy, Chief Executive Officer (principal executive officer and principal financial officer) of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 14, 2017

By: /s/ Ira Levy

Ira Levy
Chief Executive Officer
(Principal Executive Officer and
Principal Financial Officer)