

AGS COMPUTERS, INC.

ANNUAL REPORT
1971

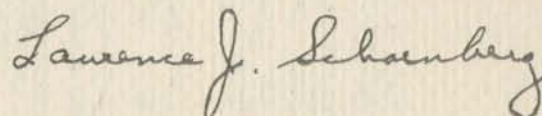
TO OUR SHAREHOLDERS

AGS has completed its first five years in business and has, in that time, established a considerable professional reputation in the information systems field. This reputation is reflected in five years of increasing revenues and the very high percentage of clients with whom we have had a long continuing relationship. AGS has continually grown by adding increments of work which can be successfully managed and integrated into our base of operations. At this moment in time, AGS is working under repetitive contracts and on multiple assignments for most of these clients.

The emphasis in 1972 will be in expanding our professional services while improving our profit margins. This will be accomplished through better utilization of our current resources. Specifically, AGS will further motivate the technical staff by making, whenever possible, their compensation depend upon project profitability. The marketing staff will offer a wider range of services in the data and information science disciplines. The major new sales thrust will be in the offering of advanced technical education courses.

Financially, AGS is well on its way to its finest first quarter in both sales and profits. Our investment in the data entry business is now represented by our 25% ownership of Players Computer, Inc. to whom we sold our interest in Duo Computers. Players' financial statement show it to be currently profitable on a monthly sales volume in excess of \$50,000.

In summary, we believe that AGS has well weathered the economic storms, has built an excellent technical and financial base, and is therefore well posed to prosper in the years to come.



LAWRENCE J. SCHOENBERG
President

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION (Note 1)

For the years ended December 31, 1971 and 1970

	<u>1971</u>	<u>1970</u>
Source of funds:		
Income (loss) before extraordinary charge	\$ 13,054	(\$ 66,178)
Depreciation (straight-line)	10,789	5,636
Working capital provided from (used in) operations, exclusive of extraordinary charge	23,843	(60,542)
Extraordinary charge	(6,000)	(101,000)
Provision for loss on noncurrent investments included therein	6,000	13,000
	<u> </u>	<u>(88,000)</u>
Working capital provided from (used in) operations	23,843	(148,542)
Decrease in deferred proprietary costs		14,188
Capital contribution by officers		56,000
Other, net	1,271	(163)
	<u>25,114</u>	<u>(78,517)</u>
Application of funds:		
Dividend (Note 4)	101,085	
Additions to fixed assets, net of dispositions (\$5,672)		45,588
Decrease in deferred income taxes		7,500
Total funds applied	<u>101,085</u>	<u>53,088</u>
Decrease in working capital	<u>(\$ 75,971)</u>	<u>(\$131,605)</u>
Changes in the components of working capital are as follows:		
Increase (decrease) in short-term securities and other investments	\$ 52,578	(\$314,193)
Decrease in notes and accounts receivable	(37,628)	
Increase (decrease) in due from officers	(100,000)	100,000
Decrease in note payable to bank	20,000	
(Increase) decrease in accrued income taxes	(15,770)	74,134
Other, net	4,849	8,454
	<u>(\$ 75,971)</u>	<u>(\$131,605)</u>

See notes to financial statements.

AGS COMPUTERS, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS (Note 1)
December 31, 1971 and 1970

ASSETS:

	<u>1971</u>	<u>1970</u>
Current assets:		
Cash	\$ 55,220	\$ 46,634
Short-term investments, at cost (approximates market)	52,578	
Accounts receivable	166,988	212,116
Notes receivable (Note 1)	7,500	
Due from officers (Note 2)		100,000
Other	<u>5,433</u>	<u>13,360</u>
Total current assets	287,719	372,110
Furniture, equipment and leasehold improvements, at cost, less accumulated depreciation and amortization (1971, \$14,874; 1970, \$6,770)	42,361	57,807
Other investments, at cost, less provision for loss (1971, \$69,000; 1970, \$63,000) (Note 2)	10,000	16,000
Other assets	<u>13,382</u>	<u>9,996</u>
	<u>\$353,462</u>	<u>\$455,913</u>

LIABILITIES:

Current liabilities:

Note payable to bank		\$ 20,000
Accounts payable and accrued expenses	\$ 80,004	84,194
Accrued income taxes	<u>18,791</u>	<u>3,021</u>
Total current liabilities	98,795	107,215

STOCKHOLDERS' EQUITY:

Common stock, par value \$.10 per share, authorized 1,000,000 shares; issued and outstanding 439,500 shares (Notes 2, 4 and 5)	334,065	435,150
Deficit	<u>(79,398)</u>	<u>(86,452)</u>
	<u>254,667</u>	<u>348,698</u>
	<u>\$353,462</u>	<u>\$455,913</u>

See notes to financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

- The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Somerset Computers, Inc., formerly Duo Computer Corp. (Duo), which was purchased in July 1970. In November 1971, the Company sold the business of Duo, together with certain fixed assets, to Players Computer, Inc. (Players) for \$9,000 of 6% notes and 5,000 shares of capital stock of Players (representing 25% of the outstanding shares). The notes and the stock have been valued at the face amount of the notes. The notes mature in twelve monthly instalments of \$750, beginning in March 1972. The Company's equity in results of operations of Players since acquisition, based upon unaudited financial statements, is not significant.

Continuing operations do not include the operating results of Duo, which have been segregated, and are set forth separately under the caption "loss from discontinued operations." Duo's 1970 loss is included from date of acquisition.
- Other investments consist of a \$50,000 participation in a \$1,000,000 note issued by Rapp Oil Corporation (Rapp), due on December 10, 1970, secured by a mortgage on certain oil leases, and a \$29,000 investment in securities (5% debentures and stock) of Shannon Properties, Inc. (Shannon). During 1970, both Rapp and Shannon ceased paying interest on their obligations to the Company and Rapp defaulted on the \$1,000,000 note; accordingly, a reserve has been provided against the investments.

The Company, together with the other participants in the \$1,000,000 note, is currently involved in litigation in order to obtain their pro rata share of the proceeds from the oil leases under mortgage, and to obtain title to the leases.

Three officers of the Company (who are also directors and majority stockholders) guaranteed to hold the Company harmless from any loss resulting from the aforementioned investments; however, it is not possible at this time to determine what action the officers will take to satisfy their guarantee should the investments prove to be worthless. The net effect of any payment to the Company will be accounted for as a contribution to capital.

In 1971, the aforementioned officers paid \$100,000 to the Company, in satisfaction of their guarantee of a note issued by Rapp which became worthless in 1970. The reimbursement net of applicable income tax effect was accounted for as a capital contribution in 1970.
- The Company and its subsidiary lease premises which they occupy under agreements that provide for the payment of minimum annual rentals aggregating approximately \$41,000 through June 30, 1975 and \$33,000 thereafter through June 30, 1979.

Certain of these premises are sublet at annual rentals of approximately \$15,000 through June 30, 1973 and \$7,800 thereafter through June 30, 1975.
- In 1971, the Board of Directors declared and the Company paid a dividend of \$101,085 (\$.23 per share). The dividend was authorized by the Board of Directors as a distribution of capital and has been so reflected in the financial statements. The three officers referred to in Note 2 own 67% of the outstanding common stock.
- The Company has a qualified stock option plan under which 20,000 shares of common stock are reserved for issuance to officers and employees at prices not lower than the fair market value at dates options are granted. Options are exercisable one year from date of grant in accordance with terms fixed by the Board of Directors, but in all cases expire five years from date of grant. During 1971, options to purchase 10,500 shares at prices ranging from \$2.50 to \$4.50 per share were terminated. At December 31, 1971, options to purchase 5,350 shares at prices ranging from \$2.00 to \$4.50 per share were outstanding and exercisable and 14,650 shares were reserved for the granting of future options.

In 1971, the Company established a nonqualified stock option plan under which 30,000 shares of common stock were reserved for issuance to Company officers and employees at prices not less than 75% of the fair market value on date of grant. Options become exercisable in three equal annual instalments commencing one year from date of grant in accordance with terms fixed by the Board of Directors, but in all cases expire ten years from date of grant. During 1971 options were granted to purchase 13,950 shares at prices ranging from \$1.00 to \$1.50 per share, and options to purchase 3,550 shares at the same price range were terminated. At December 31, 1971, options to purchase 10,400 shares at prices ranging from \$1.00 to \$1.50 per share were outstanding, of which none were exercisable, and 19,600 shares were reserved for the granting of future options.

In connection with a public offering in 1969, warrants to purchase 15,000 shares of common stock at a price of \$3.85 per share were issued to the underwriters and others. The warrants expire the earlier of May 21, 1974 or nine months after the effective date of an appropriate filing under the Securities Act of 1933 permitting the public offering of the warrants. The warrants became exercisable on May 21, 1970.
- The Company follows the policy of deferring the cost of developing proprietary programs, writing off such costs over a two-year period commencing from the time the programs are completed and offered for sale, and writing off immediately any costs related to programs which do not appear to be marketable. During 1970, costs related to a nonmarketable program were written off to expense. There were no deferred proprietary costs at December 31, 1971 and 1970.

CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND DEFICIT (Note 1)

For the years ended December 31, 1971 and 1970

	<u>1971</u>	<u>1970</u>
Revenues	\$1,018,634	\$ 965,187
Costs and expenses:		
Cost of services	569,624	605,982
Selling, general and administrative	352,481	346,343
Proprietary program costs (Note 6)	<u> </u>	<u>76,328</u>
	<u>922,105</u>	<u>1,028,653</u>
	96,529	(63,466)
Provision for taxes on income:		
Current	46,000	
Benefit attributable to operating loss carry-back	<u> </u>	<u>(32,000)</u>
Income (loss) from continuing operations before extraordinary charge	50,529	(31,466)
Loss from discontinued operations (in 1971, net of related income tax benefit, \$35,000)	<u>37,475</u>	<u>34,712</u>
Income (loss) before extraordinary charge	13,054	(66,178)
Provision for loss on investments and loans (in 1970, net of related income tax benefit, \$62,000) (Note 2)	<u>6,000</u>	<u>101,000</u>
Net income (loss)	7,054	(167,178)
Retained earnings (deficit), beginning of year	<u>(86,452)</u>	<u>80,726</u>
Deficit, end of year	<u>(\$ 79,398)</u>	<u>(\$ 86,452)</u>
Per average share of common stock:		
Income (loss) from continuing operations before extraordinary charge	\$.11	(\$.07)
Loss from discontinued operations	<u>(.08)</u>	<u>(.08)</u>
Income (loss) before extraordinary charge03	(.15)
Extraordinary charge	<u>(.01)</u>	<u>(.23)</u>
Net income (loss)	<u>\$.02</u>	<u>(\$.38)</u>

See notes to financial statements.

OFFICERS AND DIRECTORS

Lawrence J. Schoenberg	<i>President & Director</i>
Joseph Abrams	<i>Executive Vice-President, Secretary & Director</i>
Peter G. Graf	<i>Treasurer & Director</i>
Anthony F. Stepanski	<i>Senior Vice-President & Director</i>
Marcia A. Lampe	<i>Vice-President</i>
David B. Levine	<i>Vice-President</i>
Victor L. Lurie	<i>Director</i>

COUNSEL

Greenbaum, Wolff & Ernst

ACCOUNTANTS

Lybrand, Ross Bros. & Montgomery

REGISTRAR & TRANSFER AGENT

Registrar & Transfer Company

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and Stockholders of
AGS Computers, Inc.:

We have examined the consolidated balance sheet of AGS COMPUTERS, INC. and SUBSIDIARY as of December 31, 1971 and the related consolidated statements of income (loss) and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously examined and reported upon the financial statements of the Company and subsidiary for the year 1970.

In our opinion, subject to the potential increase in capital resulting from the guarantee of certain assets discussed in Note 2, the aforementioned financial statements present fairly the consolidated financial position of AGS Computers, Inc. and Subsidiary at December 31, 1971 and 1970 and the consolidated results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

LYBRAND, ROSS BROS. & MONTGOMERY

New York, March 6, 1972.