

SMITH AND SMITH, INC.  
FINANCIAL STATEMENTS  
AND  
SUPPLEMENTARY FINANCIAL INFORMATION  
YEARS ENDED SEPTEMBER 30, 2008  
AND SEPTEMBER 30, 2007

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Board of Directors  
Smith and Smith, Inc.  
1234 Main Street  
Brea, CA 92821

We have reviewed the accompanying balance sheets of Smith and Smith, Inc. as of September 30, 2008 and September 30, 2007, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management of Smith and Smith, Inc.

A review consists principally of inquiries of Company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards of the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the generally accepted accounting principles of the United States of America.

Our reviews were made for the purpose of expressing limited assurance that there are no material modifications that should be made to the financial statements in order for them to be in conformity with the generally accepted accounting principles of the United States of America. The information included in the accompanying supplementary schedules is presented only for supplementary analysis purposes. Such information has been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements, and we are not aware of any material modifications that should be made thereto.

November 12, 2008

Member, American Institute of Certified Public Accountants  
Member, California Society of Certified Public Accountants

SMITH AND SMITH, INC.

BALANCE SHEETS

ASSETS

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
<b>CURRENT ASSETS:</b>		
Cash and Cash Equivalents (Notes 1 and 2)	\$ 843,562	\$ 546,613
Restricted Cash (Note 3)	826,264	449,156
Accounts Receivable-Trade (Notes 1 and 4):		
Billed	1,203,137	2,733,556
Retentions	1,173,496	1,474,975
Costs and Estimated Profit to Date in Excess of Billings (Notes 1 and 5)	290,276	441,851
Prepaid Taxes	25,346	---
Prepaid Expense (Note 6)	84,159	70,526
Current Portion of Fixed Assets (Note 1)	<u>10,324</u>	<u>15,019</u>
Total Current Assets	4,456,564	5,731,696
 <b>EQUIPMENT, AT COST (Note 1):</b>		
Tools and Equipment	143,988	143,988
Office Furniture and Equipment	111,958	111,958
Leasehold Improvements	<u>65,163</u>	<u>65,163</u>
	321,109	321,109
Less: Accumulated Depreciation	(293,564)	(283,239)
Less: Current Portion of Fixed Assets	<u>(10,324)</u>	<u>(15,019)</u>
Net Equipment	17,221	22,851
 <b>OTHER ASSETS:</b>		
Deposits	1,000	1,000
Federal Tax Deposit (Note 1)	240,989	167,843
Employee Advances	<u>23,802</u>	<u>27,824</u>
Total Other Assets	<u>265,791</u>	<u>196,667</u>
Total Assets	<u>\$ 4,739,576</u>	<u>\$ 5,951,214</u>

See Accompanying Notes and Accountants' Review Report  
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SMITH AND SMITH, INC.

BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
<b>CURRENT LIABILITIES:</b>		
Accounts Payable-Trade (Note 7)	\$ 417,939	\$ 599,686
Accrued Expenses (Notes 8, 14, and 16)	298,748	323,483
Billings in Excess of Costs and Estimated Profit to Date (Notes 1 and 5)	304,436	471,918
Bank Line of Credit (Note 9)	---	---
Income Tax Payable	---	18,377
Anticipated Distributions (Note 10)	---	<u>233,000</u>
<b>Total Current Liabilities</b>	<b>1,021,123</b>	<b>1,646,464</b>
<b>STOCKHOLDERS' EQUITY:</b>		
Common Stock (Note 1)	2,000	2,000
Retained Earnings	<u>3,716,453</u>	<u>4,302,750</u>
<b>Total Stockholders' Equity</b>	<b><u>3,718,453</u></b>	<b><u>4,304,750</u></b>
<b>Total Liabilities and Stockholders' Equity</b>	<b><u>\$ 4,739,576</u></b>	<b><u>\$ 5,951,214</u></b>

SMITH AND SMITH, INC.  
STATEMENTS OF INCOME

	For the Years Ended September 30,	
	<u>2008</u>	<u>2007</u>
EARNED CONTRACT REVENUE	\$16,411,524	\$15,023,542
COST OF EARNED CONTRACT REVENUE:		
Material	7,365,184	3,691,534
Labor	3,685,275	3,954,009
Equipment Rental	657,139	675,676
Allocated Indirect Costs	<u>2,440,399</u>	<u>2,581,673</u>
Total Cost of Earned Contract Revenue	<u>14,147,997</u>	<u>10,902,892</u>
GROSS PROFIT	2,263,527	4,120,650
GENERAL AND ADMINISTRATIVE EXPENSE:		
Officers' Wages (Note 11)	902,800	637,400
Other General and Administrative Expense	<u>1,022,896</u>	<u>792,395</u>
Total General and Administrative Expense	<u>1,925,696</u>	<u>1,429,795</u>
INCOME FROM OPERATIONS	337,831	2,690,855
OTHER INCOME (EXPENSE) (Note 12)	<u>12,441</u>	<u>27,579</u>
INCOME BEFORE PROVISION FOR INCOME TAXES	350,272	2,718,434
PROVISION FOR INCOME TAXES (Notes 1 and 13):		
Current Tax	<u>5,254</u>	<u>40,777</u>
Total Provision for Income Taxes	<u>5,254</u>	<u>40,777</u>
NET INCOME	<u>\$ 345,018</u>	<u>\$ 2,677,657</u>

See Accompanying Notes and Accountants' Review Report  
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SMITH AND SMITH, INC.  
STATEMENTS OF CASH FLOWS

	For the Years Ended September 30,	
	2008	2007
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>		
Cash Received from Contracts Performed	\$17,850,407	\$14,583,498
Interest Received	15,693	29,446
Cash Paid to Employees and Suppliers of Goods and Services	(16,283,483)	(12,680,611)
Interest Paid	(3,252)	(1,867)
Income Taxes (Paid) Refunded	<u>(122,123)</u>	<u>(184,787)</u>
Net Cash Provided by Operating Activities	1,457,242	1,745,679
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Advances to Employees, Net of Repayments	4,022	2,178
Advances to Shareholders	<u>---</u>	<u>42,613</u>
Net Cash Provided by Investing Activities	4,022	44,791
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Bank Line of Credit Advances, Net of Repayments	---	(300,000)
"S" Corporation Distributions Paid	<u>(1,164,315)</u>	<u>(1,335,180)</u>
Net Cash (Used) by Financing Activities	<u>(1,164,315)</u>	<u>(1,635,180)</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	296,949	155,290
<b>BEGINNING CASH AND CASH EQUIVALENTS</b>	<u>546,613</u>	<u>391,323</u>
<b>ENDING CASH AND CASH EQUIVALENTS</b>	<u>\$ 843,562</u>	<u>\$ 546,613</u>

See Accompanying Notes and Accountants' Review Report  
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SMITH AND SMITH, INC.  
STATEMENTS OF CASH FLOWS

	For the Years Ended September 30,	
	<u>2008</u>	<u>2007</u>
RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net Income	\$ 345,018	\$ 2,677,657
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation	10,325	15,019
(Increase) Decrease In:		
Restricted Cash	(377,108)	582,182
Accounts Receivable:		
Billed	1,530,419	278,293
Retentions	301,479	(345,277)
Costs and Estimated Profit to Date in Excess of Billings	151,575	(209,221)
Prepaid Franchise Tax	(25,346)	---
Other Current Assets	(13,633)	68,926
Other Assets	(73,146)	(149,721)
Increase (Decrease) In:		
Accounts Payable	(181,747)	(524,645)
Accrued Expenses	(24,735)	92,776
Billings in Excess of Costs and Estimated Profit to Date	(167,482)	(746,021)
Income Taxes Payable	(18,377)	5,711
Net Cash Provided by Operating Activities	<u>\$ 1,457,242</u>	<u>\$ 1,745,679</u>
NON-CASH FINANCING ACTIVITIES:		
Total "S" Distributions on Financial Presentation	\$ 931,315	\$ 1,196,180
Less: "S" Current Year Distributions Paid	<u>(931,315)</u>	<u>(963,180)</u>
Non-Cash Anticipated "S" Distribution on Balance Sheet Date	---	233,000
Less: Prior Year Anticipated "S" Distributions Paid in Current Year	<u>(233,000)</u>	<u>(372,000)</u>
Cash (Distributions) not Included in Current "S" Distribution as Presented on Financial Statements (Payments on Account of Prior Year Anticipated Distributions)	<u>\$ (233,000)</u>	<u>\$ (139,000)</u>

See Accompanying Notes and Accountants' Review Report  
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SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - Organization and Summary of Significant Accounting Policies

Organization:

Smith and Smith, Inc., a California corporation, was incorporated on November 5, 1994. The Company operates as a specialty subcontractor in Southern California. The Company is authorized to issue 75,000 shares of no par common stock, of which 50 shares were issued and outstanding as of September 30, 2008 and September 30, 2007, with a stated value of \$40 per share. As of September 30, 2008 and September 30, 2007, respectively, the stock was held 50% by Greg and Marsha Smith, Co-Trustees under declaration of trust. At September 30, 2008 and September 30, 2007, the stock was held 50% by Daniel Smith.

Cash and Cash Equivalents:

For the purposes of reporting cash flows, the Company considers cash in operating bank accounts, demand deposits, and cash on hand as cash and cash equivalents.

Accounts Receivable-Trade and Method of Accounting for Contracts:

Accounts receivable-trade consists of billed and unbilled receivables, as well as earned amounts retained by customers pending satisfactory completion of the applicable contracts. Unbilled receivables consist of the excess of costs and estimated profit to date in excess of billings on contracts in progress.

The Company records revenues using the percentage of completion method, measured by the percentage of costs incurred to date to estimated total costs for each contract. This method is used because the Company's management considers incurred costs to be the best available measure of progress on all contracts. Changes in job performance, job conditions, and estimated profitability may result in revisions to costs and revenues after balance sheet and financial issuance dates. All contracts in progress are reviewed for cost overruns and, if total anticipated costs are expected to exceed the contract amount, the overrun is treated as a current period expense. Changes in estimated gross profits on contracts are reflected during the period in which the change in estimate is made.

General and administrative expenses are not allocated to contract cost.

The Company does not record claims for additional compensation on contracts until the contract has been revised to reflect the amount to be paid for the additional work performed. All costs related to work for which a contract revision has not been received are expensed as incurred.

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - Organization and Summary of Significant Accounting Policies (Cont.)

Reclassifications:

Certain reclassifications were made to the 2007 financial statement presentation to conform to the 2008 financial statement presentation.

Equipment:

Depreciation is recorded for financial statement presentation using the straight-line method or in accordance with Federal MACRS guidelines when not significantly different from straight-line. For tax reporting purposes, Federal and State guidelines are used. Assets are depreciated over their estimated useful lives which range from five to seven years. Depreciation expense for the years ended September 30, 2008 and September 30, 2007 was \$10,325 and \$15,019, respectively.

In accordance with the provisions of ARB 43, the Company has adopted the position that in order to properly represent the working capital of the Company, the value of equipment utilization, represented by depreciation cost, in the subsequent operating cycle is classified as a current asset.

Income Taxes:

The Company, with the consent of its stockholders, elected to be treated as an "S" corporation, effective for the year ended September 30, 1999. As such, taxable income is passed through and taxed on the stockholders' individual income tax returns. For Federal tax purposes, the Company is required to make a deposit with the Internal Revenue Service for taxes on the corporate income earned between September 30 and December 31. Taxable income is also subject to a 1.5% tax imposed by the Franchise Tax Board at the corporate level. Income taxes on business earnings and officers' wages are paid personally by the stockholders through withholding and estimated tax payments.

Management expects to issue distributions to the stockholders each year in amounts adequate to pay the taxes on the pass-through income that will be reported on their personal income tax returns (Note 10).

Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles of the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Advertisement:

The Company expenses advertising in the period incurred. Advertising and promotion expense for the years ended September 30, 2008 and September 30, 2007 was \$89,777 and \$69,961, respectively.

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - Cash and Cash Equivalents

Cash and cash equivalents consist of the following:

	<u>September 30, 2008</u>		<u>September 30, 2007</u>	
	<u>Reconciled Balance</u>	<u>Bank Statement Balance</u>	<u>Reconciled Balance</u>	<u>Bank Statement Balance</u>
City National Bank 34 Flower Street Los Angeles, CA 92999				
Checking A/C #9999999999	\$ ---	\$ ---	\$ 310,641	\$ 309,406
Checking A/C #9999999998	504,083	767,240	---	---
Savings A/C #999999997	<u>339,179</u>	<u>339,179</u>	<u>235,672</u>	<u>235,672</u>
Subtotal	843,262	1,106,419	546,313	545,078
Petty Cash	<u>300</u>	<u>---</u>	<u>300</u>	<u>---</u>
Total Cash and Cash Equivalents	<u>\$ 843,562</u>	<u>\$ 1,106,419</u>	<u>\$ 546,613</u>	<u>\$ 545,078</u>

At September 30, 2008 and September 30, 2007, the Company maintained \$1,106,419 and \$545,078, respectively, on deposit at one financial institution, of which only \$250,000 was insured by the Federal Deposit Insurance Corporation.

NOTE 3 - Restricted Cash

Restricted cash consists of amounts deposited into trust funds and pledged in lieu of retentions on individual projects. Funds are released to the Company upon final completion and acceptance of each project.

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 4 - Accounts Receivable Trade

Accounts receivable-trade consists of the following:

	<u>September 30, 2008</u>		<u>September 30, 2007</u>	
	<u>Amount</u>	<u>Percentage</u>	<u>Amount</u>	<u>Percentage</u>
Aged Receivables:				
Current	\$ 1,076,909	89.5%	\$ 2,463,802	90.1%
31 - 60 Days	---	0.0%	---	0.0%
61 - 90 Days	104,483	8.7%	250,033	9.2%
91 Days and Over	<u>21,745</u>	<u>1.8%</u>	<u>19,721</u>	<u>0.7%</u>
 Total Aged Accounts Receivable-Trade	 1,203,137	 <u>100.0%</u>	 2,733,556	 <u>100.0%</u>
 Retentions Receivable	 <u>1,173,496</u>		 <u>1,474,975</u>	
 Total Accounts Receivable-Trade	 <u>\$ 2,376,633</u>		 <u>\$ 4,208,531</u>	

The Company uses the specific identification method to charge off uncollectible trade receivables. In general, the Company considers trade receivables to be past due after thirty days; however, economic factors in the industry result in frequent delayed collections by the Company and its competitors. The Company pays close attention to trade receivables over sixty days. As of September 30, 2008 and September 30, 2007, management had determined that an allowance for doubtful accounts was not necessary.

Subsequent to September 30, 2008 and September 30, 2007, and prior to financial statement issuance, the Company received \$6,715 and \$12,508, respectively, of the 91 days and over balance and \$89,588 and \$152,022, respectively, of the 61 to 90 days and over balance. There was no bad debt expense in the years ended September 30, 2008 and September 30, 2007.

(See detailed schedules of September 30, 2008 Accounts Receivable-Trade and Retentions included in supplementary financial information.)

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 5 - Costs, Billings, and Estimated Earnings to Date on Uncompleted Contracts

Costs, billings, and estimated earnings to date on uncompleted contracts and on completed contracts final invoice not yet billed are summarized as follows:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
Costs Incurred to Date	\$11,521,379	\$18,235,300
Plus: Estimated Profit to Date	<u>1,633,290</u>	<u>4,679,539</u>
Estimated Earnings to Date	13,154,669	22,914,839
Less: Billings to Date	<u>13,168,829</u>	<u>22,944,906</u>
Net (Over)/Under Billings	<u>\$ (14,160)</u>	<u>\$ (30,067)</u>

The net (over)/under billings are presented on the balance sheets as follows:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
Costs and Estimated Profit to Date in Excess of Billings	\$ 290,276	\$ 441,851
Billings in Excess of Costs and Estimated Profit to Date	<u>304,436</u>	<u>471,918</u>
Net (Over)/Under Billings	<u>\$ (14,160)</u>	<u>\$ (30,067)</u>

(See detailed schedule as of September 30, 2008 for Contracts In Progress included in supplementary financial information.)

NOTE 6 - Prepaid Expenses

Prepaid expenses consist of the following:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
Prepaid Workers' Compensation Insurance	\$ 13,859	\$ ---
Prepaid General Liability Insurance	47,996	56,329
Prepaid Other	<u>22,304</u>	<u>14,197</u>
Total Prepaid Expenses	<u>\$ 84,159</u>	<u>\$ 70,526</u>

See Accompanying Accountants' Review Report

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 7 - Accounts Payable-Trade

Accounts payable-trade consist of amounts owed to material suppliers, subcontractors, and other direct vendors. The accounts payable agings at September 30, 2008 and September 30, 2007, were as follows:

	<u>September 30, 2008</u>		<u>September 30, 2007</u>	
	<u>Amount</u>	<u>Percentage</u>	<u>Amount</u>	<u>Percentage</u>
Current	\$ 380,303	91.0%	\$ 587,958	98.1%
31-60 Days	37,792	9.1%	11,883	2.0%
61-90 Days	---	0.0%	---	0.0%
91 days and Over	<u>(156)</u>	<u>(0.1%)</u>	<u>(155)</u>	<u>(0.1%)</u>
 Total Aged Accounts Payable-Trade	 <u>\$ 417,939</u>	 <u>100.0%</u>	 <u>\$ 599,686</u>	 <u>100.0%</u>

(See detailed schedule of September 30, 2008 Accounts Payable-Trade included in supplementary financial information.)

NOTE 8 - Accrued Expenses

Accrued expenses consist of the following:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
Accrued Union Dues, Payroll and Related Liabilities	\$ 198,748	\$ 223,483
Pension Plan Contribution Payable (Note 14)	<u>100,000</u>	<u>100,000</u>
 Total Accrued Expenses	 <u>\$ 298,748</u>	 <u>\$ 323,483</u>

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 9 - Bank Line of Credit

The Company has a \$1,000,000 revolving line of credit extended by City National Bank, 34 Flower Street, Los Angeles, CA 92999, secured by substantially all assets of the Company except accounts receivable, and personally guaranteed by each of the stockholders. Terms of repayment call for interest payments payable monthly at the bank's prime rate. As of September 30, 2008 and September 30, 2007, there was no outstanding balance. The line of credit matured on April 1, 2008 and was renewed. As of September 30, 2008 and September 30, 2007, the Company was in compliance with the bank's financial covenants as stated in loan agreement.

NOTE 10 - Anticipated Distributions

Anticipated distributions reflect management's intention to distribute earnings to its stockholders to pay income taxes on Company income being passed through to the stockholders and taxed on their personal returns. "S" distributions were made in direct proportion to ownership of capital at the dates of accrual. Anticipated "S" distributions as of September 30, 2008 were as follows:

	September 30, 2008		
	Greg Smith	Daniel Smith	Total
Anticipated "S" Distributions	\$ ---	\$ ---	\$ ---

Anticipated "S" distributions as of September 30, 2007 were as follows:

	September 30, 2007		
	Greg Smith	Daniel Smith	Total
Anticipated "S" Distributions	\$ 116,500	\$ 116,500	\$ 233,000

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 11 - Officers' Wages

Officers' wages, excluding deferred compensation, consist of the following:

	For the Years Ended September 30,	
	<u>2008</u>	<u>2007</u>
Greg Smith	\$ 480,000	\$ 347,200
Daniel Smith	<u>422,800</u>	<u>290,200</u>
Total Officers' Wages	<u>\$ 902,800</u>	<u>\$ 637,400</u>

NOTE 12 - Other Income (Expense)

Other income (expense) consists of the following:

	For the Years Ended September 30,	
	<u>2008</u>	<u>2007</u>
Interest Income	\$ 15,693	\$ 29,446
Interest Expense	<u>(3,252)</u>	<u>(1,867)</u>
Total Other Income (Expense)	<u>\$ 12,441</u>	<u>\$ 27,579</u>

NOTE 13 - Provision for Income Taxes

A reconciliation of items between the income tax provision for the year and the amount of income tax expense that would result from applying Federal and State statutory rates to pre-tax income follows:

	For the Years Ended September 30,	
	<u>2008</u>	<u>2007</u>
Tax Expense at Statutory Rates	\$ 5,254	\$ 40,777
Total Provision for Income Tax	<u>\$ 5,254</u>	<u>\$ 40,777</u>

There were no differences between the tax basis of assets and liabilities and their financial reporting amounts for the years ended September 30, 2008 and September 30, 2007, which would have resulted in deferred income taxes.

(See detailed schedule of September 30, 2008 Taxable Income included in the supplementary financial information.)



SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 14 - Profit Sharing Plans

During the year ended September 30, 2004, the Company merged its Money Purchase Pension Plan and Profit Sharing Plan into a single profit sharing plan that covers all eligible non union employees who meet the qualifications. Provisions of the plan allow for exclusion of some highly compensated employees. The Company's management determines, at its discretion, the Company's annual contribution, if any, to the plan.

The accrued profit sharing contribution for the year ended September 30, 2008 is \$100,000 (Note 8), and funding is due by June 15, 2009. The accrued profit sharing contribution for the year ended September 30, 2007 was \$100,000 (Note 8). The profit sharing expense for the years ended September 30, 2008 and September 30, 2007 was \$102,500 and \$102,816, respectively.

NOTE 15 - Related Party Transactions

The Company rents its office facilities on a month-to-month basis from a related party. The annual rent paid to the related party for the years ended September 30, 2008 and September 30, 2007 was \$57,188 and \$57,188, respectively.

The Company leases equipment from Jones and Smith, Inc., a company related by some common ownership. The equipment rental expense for equipment leased from the related party for the year ended September 30, 2008 and September 30, 2007 was \$540,320 and \$577,815, respectively. As of September 30, 2008 and September 30, 2007, the payables to the related party were \$33,850 and \$42,645, respectively.

NOTE 16 - Concentrations

During the year ended September 30, 2008, the Company earned approximately 51% of its revenue from three customers. During the year ended September 30, 2007, the Company earned approximately 23% of its revenue from two customers. The receivables for those customers at September 30, 2008 and September 30, 2007 totaled \$436,313 and \$593,509, respectively. Additionally, \$171,237 and \$378,703 were retentions receivable at September 30, 2008 and September 30, 2007 from the same customers.

During the year ended September 30, 2008, the Company purchased approximately 72% of its direct job materials from two suppliers. As of September 30, 2008, the amount due the suppliers and included in accounts payable was \$236,626. During the year ended September 30, 2007, the Company purchased approximately 50% of its direct job materials from three suppliers. As of September 30, 2007, the amount due the suppliers and included in accounts payable was \$255,018.

SMITH AND SMITH, INC.  
NOTES TO FINANCIAL STATEMENTS

NOTE 16 - Concentrations (Cont.)

During the years ended September 30, 2008 and September 30, 2007, the Company used field labor, of which 100% was subject to collective bargaining agreements. The Construction Laborers Union contract expires June 2010. The Company intends to renew the union contract when it expires.

Management does not consider any of the concentrations to be indicative of unusual risk.

NOTE 17 - Contingencies

The Company has the usual obligations of a contractor for performance in connection with contracts for work performed and to be performed. Management does not anticipate any significant losses in connection with Company obligations.

The Company is subject to legal proceedings and claims which arise in the ordinary course of its business. In the opinion of management, the amount of ultimate liability with respect to those actions is not expected to materially affect the financial position of the Company.

NOTE 18 - Backlog

Backlog represents the amount of revenue the Company expects to realize from work to be performed on uncompleted contracts at year end. Backlogs for the years ended September 30, 2008 and September 30, 2007, are summarized as follows:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
Total Approved Contract Amounts for Uncompleted Contracts	\$18,170,429	\$34,133,181
Less: Contract Revenue Earned on Uncompleted Contracts	<u>12,033,892</u>	<u>16,906,008</u>
Backlog Balance	<u>\$ 6,136,537</u>	<u>\$17,227,173</u>

(See detailed schedule as of September 30, 2008, for Schedule of Contracts and Contracts in Progress included in supplementary financial information.)

SUPPLEMENTARY FINANCIAL INFORMATION

SMITH AND SMITH, INC.  
SCHEDULES OF OTHER GENERAL AND ADMINISTRATIVE EXPENSE,  
AND INDIRECT COSTS

	For the Years Ended	
	September 30,	
	<u>2008</u>	<u>2007</u>
<b>OTHER GENERAL AND ADMINISTRATIVE EXPENSE:</b>		
Administrative Wages and Related Expense	\$ 300,203	\$ 293,063
Professional and Legal Services	42,880	35,306
Pension Plan Expense	102,500	102,816
Office Expense	71,180	71,419
Telephone, Utilities and Rent	113,379	113,949
Advertising and Promotion	89,777	69,961
Depreciation	891	2,115
Net Indirect Cost (See Schedule Below)	<u>302,086</u>	<u>103,766</u>
 Total Other General and Administrative Expense	 <u>\$ 1,022,896</u>	 <u>\$ 792,395</u>
 <b>INDIRECT COSTS:</b>		
Union Benefits	\$ 1,200,126	\$ 1,247,909
Payroll Tax and Insurance	369,267	361,349
Workers' Compensation Insurance	226,564	272,643
Yard Expenses, Shop Supplies and Maintenance	277,851	284,399
General Liability Insurance	200,005	190,250
Depreciation	9,434	12,904
Equipment Repair and Maintenance	144,071	162,667
Vehicle Expense	149,045	113,269
Previously Closed Job Costs (Income)	44,613	(109,929)
Supervisor Wages	86,644	85,010
Scaffolding and Pallet Expense	29,475	50,746
Licenses and Permits	5,390	14,222
Allocated Indirect Costs	<u>(2,440,399)</u>	<u>(2,581,673)</u>
 Net Indirect Costs Included in Other General and Administrative Expense (Above)	 <u>\$ 302,086</u>	 <u>\$ 103,766</u>

SMITH AND SMITH, INC.  
SCHEDULES OF WORKING CAPITAL

	September 30,	
	2008	2007
Beginning Working Capital:		
Current Assets	\$ 5,731,696	\$ 5,936,290
Current Liabilities	1,646,464	3,215,030
Beginning Working Capital	\$ 4,085,232	\$ 2,721,260
Ending Working Capital:		
Current Assets	\$ 4,456,564	\$ 5,731,696
Current Liabilities	1,021,123	1,646,464
Ending Working Capital	\$ 3,435,441	\$ 4,085,232

SMITH AND SMITH, INC.  
 BILLED ACCOUNTS RECEIVABLE-TRADE AGING AND RETENTIONS  
 September 30, 2008

	<u>BILLED</u>					<u>Retentions</u>
	<u>Total</u>	<u>Current</u>	<u>31-60 Days</u>	<u>61-90 Days</u>	<u>91 Days and Over</u>	
1510 McCarthy Building 24760 Stewart Street Loma Linda, CA 92354	\$ 85,606	\$ 85,606	\$ ---	\$ ---	\$ ---	\$ 87,106
1534 Bomel Construction Co. 8195 E. Kaiser Boulevard Anaheim Hills, CA 92808	98,129	98,129	---	---	---	23,426
1535 Edge Development, Inc. 27368 Via Industrial #101 Temecula, CA 92590	431,084	431,084	---	---	---	47,898
1550 T.B. Penick & Sons, Inc. 9747 Olson Drive San Diego, CA 92121	109,620	109,620	---	---	---	14,690
1552 Day Construction Co. 3188-C Airway Avenue Costa Mesa, CA 92626-4652	226,847	220,133	---	---	6,714	25,205
Others (Under \$85,000)	<u>251,851</u>	<u>132,337</u>	<u>---</u>	<u>104,483</u>	<u>15,031</u>	<u>975,171</u>
Totals	<u>\$1,203,137</u>	<u>\$1,076,909</u>	<u>\$ ---</u>	<u>\$ 104,483</u>	<u>\$ 21,745</u>	<u>\$1,173,496</u>
Percentages	<u>100.0%</u>	<u>89.5%</u>	<u>0.0%</u>	<u>8.7%</u>	<u>1.8%</u>	

SMITH AND SMITH, INC.  
 ACCOUNTS PAYABLE-TRADE AGING  
 September 30, 2008

	<u>Total</u>	<u>Current</u>	<u>31-60 Days</u>	<u>61-90 Days</u>	<u>91 Days and Over</u>
Construction Pros, Inc. 6131 Yorkshire Road Chino, CA 91710	\$ 26,362	\$ 26,362	\$ ---	\$ ---	\$ ---
My Company, Inc. 123 Tyler Street Riverside, CA 92509	33,850	33,850	---	---	---
Joe's Supply P.O. Box 238 Stanton, CA 90680	128,626	128,626	---	---	---
Rancho Ready Mix Beaumont, CA 92228	108,000	108,000	---	---	---
Others (Under \$26,000)	<u>121,101</u>	<u>83,465</u>	<u>37,792</u>	<u>---</u>	<u>(156)</u>
Totals	<u>\$ 417,939</u>	<u>\$ 380,303</u>	<u>\$ 37,792</u>	<u>\$ ---</u>	<u>\$ (156)</u>
Percentages	<u>100.0%</u>	<u>91.0%</u>	<u>9.1%</u>	<u>0.0%</u>	<u>(0.1%)</u>

SMITH & SMITH, INC.  
 CONTRACTS IN PROGRESS  
 PERCENTAGE OF COMPLETION BASIS  
 As of September 30, 2008

Contract Number	1	2	3	4	5	6	7	8	9	10	11	12
	Total Revised Contract Price	Estimated Total Costs at Completion	Estimated Profit (Loss) at Completion 1-2(2-1)	Costs Incurred To Date	% Complete 4/2	Profit To Date 5+3	Amount Earned To Date 6+4	Amount Billed To Date	Billing in Excess of Costs and Profit to Date 8-7	Costs and Profit to Date In Excess of Billings 7-8	Estimated Costs To Complete 2-4	Contract Balance 1-8

CONTRACTS IN PROGRESS:

1488 Victor Valley Jr High	\$ 899,346	\$ 514,774	\$ 184,571	\$ 499,562	97.0%	\$ 179,034	\$ 678,596	\$ 681,699	\$ 3,103	\$ -	\$ 15,212	\$ 17,646
1498 Fire Station #64	1,172,159	994,248	177,911	983,263	98.9%	175,954	1,159,217	1,136,994	-	22,223	10,985	35,165
1510 LLU Centennial Complex PHS-1	917,983	726,034	191,949	695,137	95.7%	183,695	878,832	871,057	-	7,775	30,897	46,926
1525 Saddleback Gyms	1,560,700	1,507,770	52,930	1,473,601	97.7%	51,713	1,525,314	1,516,800	-	8,514	34,169	43,900
1528 Louis Vandermoelen Elem	386,300	280,328	105,972	268,684	95.8%	101,521	370,205	380,675	10,470	-	11,644	5,625
1532 DeBell Clubhouse	396,778	306,652	90,126	219,624	71.6%	64,530	284,154	230,860	-	53,274	87,028	165,898
1535 Murrleta Mesa High School	6,975,817	6,501,693	474,124	5,553,511	85.4%	404,902	5,958,413	6,128,243	169,830	-	948,182	847,574
1536 OCSJ Sludge Facility	984,800	773,927	210,873	7,157	0.9%	1,898	9,055	-	-	-	766,770	984,800
1540 Firmore WPT #2	293,940	233,615	60,325	112,666	48.2%	29,077	141,743	186,580	44,837	-	120,949	107,380
1543 LCCD-Bakery, CP & ED Bldgs	340,430	215,623	124,807	100,272	46.5%	58,035	158,307	198,430	40,123	-	115,351	142,000
1549 SCRRRA East Maintenance Facility	371,200	289,407	81,793	28,782	9.9%	8,098	36,880	30,000	-	6,880	260,625	341,200
1550 Mtn View Alt High School	209,700	142,386	67,312	77,013	54.1%	36,416	113,429	146,900	33,471	-	65,375	62,800
1552/553 Paramount/ La Puente	474,769	365,463	109,306	364,463	99.7%	108,978	473,441	418,729	-	54,712	1,000	56,040
1556 Fox Theater	379,209	303,500	75,709	127,696	42.1%	31,873	159,569	80,175	-	79,394	175,804	289,034
Others (Under \$200,000)	3,007,299	2,342,469	664,830	59,409	-	27,328	86,737	89,339	2,602	-	2,283,060	2,917,960
	18,170,429	15,487,891	2,672,538	10,570,840		1,483,052	12,033,892	12,096,501	304,436	241,827	4,927,051	6,073,928

COMPLETED CONTRACT FINAL INVOICE NOT YET BILLED:

1527 San Marcos Middle School	930,997	799,645	131,352	799,645	100.0%	131,352	930,997	917,072	-	13,925	-	13,925
Others (Under \$200,000)	189,780	150,894	38,886	150,894		38,886	189,780	155,256	-	34,524	-	34,524
	1,120,777	950,539	170,238	950,539		170,238	1,120,777	1,072,328	-	48,449	-	48,449
TOTALS	\$ 19,291,206	\$ 16,448,430	\$ 2,842,776	\$ 11,521,379		\$ 1,633,290	\$ 13,154,669	\$ 13,168,829	\$ 304,436	\$ 280,276	\$ 4,927,051	\$ 6,122,377

See Accompanying Notes and Accountants' Review Report  
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SMITH & SMITH, INC.  
SCHEDULE OF CONTRACTS  
For the Year Ended September 30, 2008

Contract Description & Location	Contract Totals			Before September 30, 2007			For Year Ended September 30, 2008		
	REVENUES EARNED	COST OF REVENUES	GROSS PROFIT (LOSS)	REVENUES EARNED	COST OF REVENUES	GROSS PROFIT (LOSS)	REVENUES EARNED	COST OF REVENUES	GROSS PROFIT (LOSS)
<b>CONTRACTS IN PROGRESS:</b>									
1488 Victor Valley Jr High	\$ 678,596	\$ 499,562	\$ 179,034	\$ 606,502	\$ 438,471	\$ 168,031	\$ 72,094	\$ 61,091	\$ 11,003
1498 Fire Station #64	1,159,217	983,263	175,954	742,375	558,038	184,337	416,842	425,225	(8,383)
1510 LLU Centennial Complex PHS-1	878,832	695,137	183,695	230,767	160,678	70,089	648,065	534,459	113,606
1525 Saddleback Gyms	1,525,314	1,473,601	51,713	163,351	110,794	52,557	1,361,963	1,362,807	(844)
1528 Louis Vandermolen Elem	370,205	268,684	101,521	6,226	4,365	1,861	363,979	264,319	99,660
1532 Debell Clubhouse	284,154	219,624	64,530	-	-	-	284,154	219,624	64,530
1535 Murrieta Mesa High School	5,958,413	5,553,511	404,902	-	-	-	5,958,413	5,553,511	404,902
1536 OCSD Sludge Facility	9,055	7,157	1,898	-	-	-	9,055	7,157	1,898
1540 Filmore WPT #2	141,743	112,666	29,077	-	-	-	141,743	112,666	29,077
1543 LCCD-Bakery, CP & ED Bldgs	158,307	100,272	58,035	-	-	-	158,307	100,272	58,035
1549 SCRRA East Maintenance Facility	36,880	28,782	8,098	-	-	-	36,880	28,782	8,098
1550 Mtn View Alt High School	113,429	77,013	36,416	-	-	-	113,429	77,013	36,416
1552/1553 Paramount/ La Puente	473,441	364,463	108,978	-	-	-	473,441	364,463	108,978
1556 Fox Theater	159,569	127,696	31,873	-	-	-	159,569	127,696	31,873
Others (Under \$200,000)	86,737	69,409	27,328	45,555	35,229	10,326	41,182	24,180	17,002
	<u>12,033,892</u>	<u>10,570,840</u>	<u>1,463,052</u>	<u>1,794,776</u>	<u>1,307,575</u>	<u>487,201</u>	<u>10,239,116</u>	<u>9,263,265</u>	<u>975,851</u>
<b>COMPLETED CONTRACTS FINAL INVOICE NOT YET BILLED:</b>									
1527 San Marcos Middle School	930,997	799,645	131,352	121,163	96,348	25,815	809,834	704,297	105,537
Others (Under \$200,000)	189,780	150,894	38,886	-	-	-	189,780	150,894	38,886
	<u>1,120,777</u>	<u>950,539</u>	<u>170,238</u>	<u>121,163</u>	<u>95,348</u>	<u>25,815</u>	<u>999,614</u>	<u>855,191</u>	<u>144,423</u>
<b>CONTRACTS COMPLETED:</b>									
1436 Heritage High School	8,018,462	6,285,329	1,733,133	7,831,095	6,086,831	1,744,264	187,367	196,498	(11,131)
1447 San Juan Hills HS	3,882,864	2,796,481	1,086,383	3,857,368	2,787,522	1,069,846	25,486	8,959	16,537
1474 Henry J Mills WTP	526,736	284,567	242,169	230,849	152,268	78,581	295,887	132,289	163,588
1480 Rubidoux Fleet Services Bldg	322,195	241,191	81,004	320,249	239,731	80,518	1,946	1,460	486
1496 Hemet Professional Dev Svc Ctr	283,081	184,224	98,857	270,947	173,958	96,989	12,134	10,266	1,868
1501 Genomics Bldg	970,312	671,826	298,486	42,660	33,410	9,250	927,652	638,416	289,236
1515 Texas Street Pump Station	252,239	187,098	65,141	992	781	211	251,247	186,317	64,930
1518 Anaheim HS - 2 Story	1,233,389	971,181	262,208	174,801	133,118	41,683	1,058,588	838,063	220,525
1520 Irvine Station Parking Structure	264,000	210,084	53,916	-	-	-	264,000	210,084	53,916
1534 Promenade East P/S	468,521	331,108	137,413	-	-	-	468,521	331,108	137,413
1541 AB Miller	217,541	253,702	(36,161)	-	-	-	217,541	253,702	(36,161)
Others (Under \$200,000)	2,178,347	1,778,687	399,660	715,932	538,318	177,614	1,462,415	1,240,369	222,046
	<u>18,617,687</u>	<u>14,175,478</u>	<u>4,442,209</u>	<u>13,444,893</u>	<u>10,145,937</u>	<u>3,298,956</u>	<u>5,172,794</u>	<u>4,029,541</u>	<u>1,143,253</u>
<b>GRAND TOTALS</b>	<b>\$ 31,772,366</b>	<b>\$ 25,695,857</b>	<b>\$ 6,075,499</b>	<b>\$ 15,360,832</b>	<b>\$ 11,548,860</b>	<b>\$ 3,811,972</b>	<b>\$ 16,411,524</b>	<b>\$ 14,147,987</b>	<b>\$ 2,263,527</b>

See Accompanying Notes and Accountants' Review Report  
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SMITH AND SMITH, INC.  
 INCOME TAX COMPUTATION  
 For the Year Ended September 30, 2008

	<u>Per Tax Return</u>	<u>Deferred Income</u>
INCOME TAXES:		
Earnings Before Income Taxes	\$ 350,272	\$ ---
California Franchise Tax Rate	<u>1.5%</u>	<u>1.5%</u>
Total Current and Deferred Franchise Tax	5,254	---
Less: Prepaid Franchise Tax	<u>(30,600)</u>	<u>---</u>
Income Taxes Payable (Prepaid)	<u>\$ (25,346)</u>	<u>\$ ---</u>

There are no material differences between State and Federal taxable pass-through income to the stockholders.