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PUBLICARD INC  
Form 10-Q  
May 11, 2001

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549  
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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 MARCH 31, 2001

OR

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

For the transition period from \_\_\_ to \_\_\_.

COMMISSION FILE NUMBER 0-29794

PUBLICARD, INC.  
(Exact name of registrant as specified in its charter)

PENNSYLVANIA

23-09

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer

620 FIFTH AVENUE, 7TH FLOOR, NEW YORK, NY  
(Address of principal executive offices)

100  
(Zip

Registrant's telephone number, including area code: (212) 651-3102

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   
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Number of shares of Common Stock outstanding as of May 11, 2001: 24,237,402

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PART I. FINANCIAL INFORMATION  
 ITEM 1. FINANCIAL STATEMENTS

PUBLICARD, INC.  
 AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEETS AS OF  
 MARCH 31, 2001 AND DECEMBER 31, 2000  
 (IN THOUSANDS EXCEPT SHARE DATA)

	MARCH 31, 2001 ----	DECEMBER 31, 2000 ----
	(unaudited)	
ASSETS		
Current assets:		
Cash, including short-term investments of \$12,899 in 2001 and \$16,820 in 2000	\$ 13,138	\$ 17,040
Trade receivables, less allowance for doubtful accounts (2001 - \$108, 2000 - \$89)	1,512	1,630
Inventories	2,194	1,610
Other	440	460
	-----	-----
Total current assets	17,284	20,750
	-----	-----
Equipment and leasehold improvements, net	1,540	1,620
Goodwill	8,111	8,760
Other assets	6,056	6,030
	-----	-----
	\$ 32,991	\$ 37,170
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	\$ 1,157	\$ 1,080
Accrued liabilities	6,108	6,510
	-----	-----
Total current liabilities	7,265	7,590
Other non-current liabilities	5,896	6,010
	-----	-----
Total liabilities	13,161	13,600
	-----	-----
Shareholders' equity:		
Class A Preferred Stock, Second Series, no par value: 1,000 shares authorized; 790 issued and outstanding	3,950	3,950
Common shares, \$0.10 par value: 40,000,000 shares authorized; 24,237,402 shares issued as of March 31, 2001 and December 31, 2000	2,424	2,424
Additional paid-in capital	107,265	107,300
Accumulated deficit	(93,519)	(90,010)
Other comprehensive loss	(220)	-
Unearned compensation	(70)	(80)

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Total shareholders' equity

-----  
19,830  
-----  
\$ 32,991  
=====

-----  
23,57  
-----  
\$ 37,17  
=====

The accompanying notes to consolidated financial statements  
are an integral part of these balance sheets.

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PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF INCOME (LOSS)  
FOR THREE MONTHS ENDED MARCH 31, 2001 AND 2000  
(IN THOUSANDS EXCEPT SHARE DATA)  
(UNAUDITED)

	2001 ----	2000 ----
Net sales	\$ 1,520	\$ 1,551
Cost of sales	832 -----	738 -----
Gross margin	688 -----	813 -----
Operating expenses:		
General and administrative	1,302	1,793
Sales and marketing	1,293	1,842
Product development	922	802
Stock compensation	15	426
Goodwill amortization	660	660
	----- 4,192	----- 5,523
Loss from operations	(3,504) -----	(4,710) -----
Other income (expenses):		
Interest income	207	188
Interest expense	(19)	(38)
Cost of pensions - non-operating	(216)	(211)
Other income	23	--
	----- (5)	----- (61)
Net loss	\$ (3,509) =====	\$ (4,771) =====
Basic loss per common share	\$ (.14) =====	\$ (.21) =====

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Weighted average shares outstanding	24,237,402 =====	22,681,195 =====
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The accompanying notes to the consolidated financial statements are an integral part of these statements.

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PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
FOR THE THREE MONTHS ENDED MARCH 31, 2001  
(IN THOUSANDS EXCEPT SHARE DATA)  
(UNAUDITED)

	Class A Preferred Stock -----	Common Shares ----- Shares Issued -----	Amount -----	Additional Paid-in Capital -----	Accu- De -----
Balance - December 31, 2000	\$3,950	24,237,402	\$2,424	\$ 107,300	\$ (
Private placement costs	--	--	--	(35)	
Amortization of unearned compensation	--	--	--	--	
Comprehensive Income:					
Net loss	--	--	--	--	
Foreign currency translation adjustment	--	--	--	--	
	-----	-----	-----	-----	-----
Balance - March 31, 2001	\$3,950 =====	24,237,402 =====	\$2,424 =====	\$ 107,265 =====	\$ (

	Share- holders' Equity -----	Other Comprehen- sive Income (loss) -----
Balance - December 31, 2000	\$ 23,578	\$ --
Private placement costs	(35)	--
Amortization of unearned compensation	16	--
Comprehensive Income:		
Net loss	(3,509)	(3,509)
Foreign currency translation adjustment	(220)	(220)

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	-----	-----
Balance - March 31, 2001	\$ 19,830	\$ (3,729)
	=====	=====

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

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PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE THREE MONTHS ENDED MARCH 31, 2001 AND 2000  
(IN THOUSANDS)  
(UNAUDITED)

	2001	2000
	----	----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Loss from continuing operations	\$ (3,509)	\$ (4,7
Adjustments to reconcile loss to net cash		
Used in continuing operations		
Goodwill amortization	660	6
Stock compensation expense	16	4
Depreciation	70	
Changes in operating assets and liabilities	(1,154)	(1,0
	-----	-----
Net cash used in continuing operations	(3,917)	(4,6
Loss from discontinued operations		
Non-cash charges	--	4
Change in net assets of discontinued operations	(91)	(1,5
	-----	-----
Net cash used in discontinued operations	(91)	(1,1
	-----	-----
Net cash used in operating activities	(4,008)	(5,7
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(14)	(1
Investment in TecSec, Incorporated	(25)	
	-----	-----
Net cash used in continuing operations	(39)	(1
Proceeds from discontinued operations	176	
Capital expenditures from discontinued operations	--	(1
	-----	-----
Net cash provided by (used in) discontinued operations	176	(1
	-----	-----
Net cash provided by (used in) operating activities	137	(3
	-----	-----
Cash flows from financing activities:		

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Issuance of common shares pursuant to stock option exercises	--	7
Costs incurred from private placement of Class A Preferred Stock	(35)	
Repayment of notes payable from discontinued operations	--	(
	-----	-----
Net cash provided by (used in) financing activities	(35)	7
	-----	-----
Effect of exchange rate changes on cash and cash equivalents	(5)	
	-----	-----
Net decrease in cash	(3,911)	(5,3
Cash - beginning of period	17,049	18,2
	-----	-----
Cash - end of period	\$ 13,138	\$ 12,9
	=====	=====

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

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PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF THE BUSINESS

PublicARD, Inc. ("PublicARD" or the "Company") was incorporated in the Commonwealth of Pennsylvania in 1913. PublicARD entered the smart card industry in early 1998, and began to develop solutions for the conditional access, security, payment system and data storage needs of industries utilizing smart card technology. In 1998 and 1999, the Company made a series of acquisitions to enhance its position in the smart card industry. In March 2000, PublicARD's Board of Directors, together with its management team, determined to integrate its operations and focus on deploying smart card solutions which facilitate secure access and transactions. To effect this new business strategy, in March 2000, the Board of Directors adopted a plan of disposition pursuant to which the Company divested its non-core operations. See Note 5 for a discussion on the disposition plan.

PublicARD, through its Infineer subsidiaries, is a smart card technology company, which provides infrastructure products and solutions to facilitate secure access and transactions. The Company's products and solutions include integrated circuits, smart card readers and software systems. PublicARD sells its products and solutions to customers for deployment in enterprise and on-line security and transactions management applications. In May of 2000, PublicARD unveiled its new corporate brand of Infineer bringing together its subsidiaries located in Northern Ireland and the United States under a single focus in an effort to capitalize on its core competencies and growth opportunities in smart card technology.

BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements reflect all

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normal and recurring adjustments that are, in the opinion of management, necessary to present fairly the financial position of the Company and its subsidiary companies as of March 31, 2001 and the results of their operations and cash flows for the three months ended March 31, 2001 and 2000. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted. These financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Form 10-K for the year ended December 31, 2000, as amended.

### EARNINGS (LOSS) PER COMMON SHARE

Basic net income (loss) per common share is based on net income divided by the weighted average number of common shares outstanding during each period. Diluted net income (loss) per common share assumes issuance of the net incremental shares from stock options, warrants and convertible preferred stock at the later of the beginning of the year or date of issuance. Diluted net income (loss) per share was not computed for 2001 and 2000 as the effect of stock options, warrants and convertible preferred stock were antidilutive.

### RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", subsequently amended by SFAS Nos. 137 and 138. SFAS No. 133 establishes accounting and reporting standards for derivative financial instruments and hedging activities related to those instruments, as well as other hedging activities. To date, the Company has had no investments in derivative financial instruments and has not engaged in hedging activities. Accordingly, the Company has determined the application of SFAS No. 133 does not have an impact on its financial position, results of operations or cash flows.

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PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### INVENTORIES

Inventories are stated at lower of cost (first-in, first-out method) or market. The Company evaluates the need to record adjustments for impairment of inventory on a quarterly basis. Inventory in excess of the Company's estimated usage requirements is written down to its estimated net realizable value. Inherent in the estimates of net realizable value are managements estimates related to the Company's production schedules, customer demand, possible alternative uses and the ultimate realization of potentially excess inventory. Inventories as of March 31, 2001 and December 31, 2000 consisted of the following (in thousands):

	2001	2000
	-----	-----
Raw materials and supplies	\$ 696	\$ 750
Finished goods	1,498	867
	-----	-----
	\$2,194	\$1,617

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NOTE 2 - ACQUISITIONS

In December 2000, the Company acquired a 3.5% ownership interest in TecSec, Incorporated ("TecSec") for \$5.0 million. TecSec, a Virginia corporation, develops and markets smart card-based encryption products and solutions, which will enable the next generation information security for the enterprise, multi-enterprise e-business and other markets. The TecSec investment has been accounted for at cost and could be subject to write-down in future periods if it is determined that the investment is impaired and not recoverable.

NOTE 3 - STOCK OPTIONS

In February 2001, the Company concluded a stock option re-pricing program whereby a total of approximately 3.3 million stock options were cancelled. Pursuant to the program, employees and directors voluntarily elected to cancel stock options held with an exercise price that exceeded \$4.81. In return, the Company will grant an equal number of replacement stock options on August 20, 2001. The replacement stock options will generally contain the same terms and conditions of the cancelled stock options and will have an exercise price equal to the closing price of the Company's common stock on August 20, 2001.

NOTE 4 - SEGMENT DATA

As a result of the disposition of certain operations (See Note 5) and because the Company predominantly operates in one industry, that being the deployment of smart card solutions which facilitate secure access and transactions, the Company reports as a single segment. Sales by geographical areas for the three months ended March 31, 2001 and 2000 are as follows (in thousands):

	2001 -----	2000 -----
United States	\$ 635	\$ 164
Europe	822	1,261
Far East	27	61
Rest of world	36	65
	-----	-----
	\$1,520	\$1,551
	=====	=====

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company has operations in the United States and United Kingdom. Identifiable assets by country as of March 31, 2001 and December 31, 2000 are as follows (in thousands):

2001

2000



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	----	----
United States	\$22,430	\$25,547
United Kingdom	2,450	2,866
	-----	-----
	\$24,880	\$28,413
	=====	=====

NOTE 5 - DISCONTINUED OPERATIONS

In March 2000, the Company's Board of Directors adopted a plan to dispose of the operations of the Company's Greenwald Industries Inc. ("Greenwald"), Greenwald Intellicard, Inc. (Greenwald Intellicard), Greystone Peripherals, Inc. ("Greystone") and Amazing Smart Card Technologies, Inc. ("Amazing") subsidiaries. These subsidiaries design, manufacture and distribute mechanical and smart card laundry solutions, hard disk duplicators and smart cards. In the fourth quarter of 1999, the Company recorded a loss of \$2.0 million related to the disposition plan, net of the expected gain on the disposition of these businesses. The loss provision was based on estimates of the proceeds expected to be realized on the dispositions and the results of operations through the disposition or wind-down dates.

On June 29, 2000, the Company completed the sale of substantially all of the assets of Greenwald and Greenwald Intellicard to The Eastern Company ("Eastern") for \$22.5 million in cash less \$1.75 million held in escrow to secure the payment of certain indemnification obligations. As part of the transaction, Eastern assumed certain liabilities of Greenwald and Greenwald Intellicard, including certain contractual liabilities, accounts payable and accrued liabilities. The Company has substantially completed the wind-down of the operations of Amazing and Greystone including the sale of certain assets and the licensing of certain intellectual property.

Following the substantial completion of the disposition plans, the Company revised its estimates of proceeds and expenses and recognized a gain of \$4.3 million in the third quarter of 2000 primarily related to the sale of Greenwald and Greenwald Intellicard. The amounts the Company will ultimately realize from its discontinued operations could differ from the amounts estimated and could therefore result in additional charges or gains in future periods.

The results of the operations of Greenwald, Greenwald Intellicard, Amazing and Greystone have been reflected as discontinued operations. Summarized balance sheet information with respect to the discontinued operations as of March 31, 2001 is as follows (in thousands):

Current assets	\$ 140
Non-current assets	2,223
Current liabilities and disposition	(3,895)
	-----
reserves	
Net assets of discontinued operations	\$(1,532)
	=====

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE 6 - SUPPLEMENTAL CASH FLOW INFORMATION

Changes in operating assets and liabilities reflected in the Consolidated Statements of Cash Flows are net of acquisitions of businesses and consisted of the following for the three months ended March 31, 2001 and 2000 (in thousands):

	2001	2000
	-----	-----
Trade receivables	\$ 54	\$ (267)
Inventories	(618)	(492)
Other current assets	(120)	158
Other assets	(5)	(78)
Trade accounts payable	101	171
Accrued liabilities	(457)	(724)
Other non-current liabilities	(109)	207
	-----	-----
	\$ (1,154)	\$ (1,025)
	=====	=====

Cash paid for interest during 2000 was \$6,000 and no cash was paid for interest in 2001. No income taxes were paid in 2000 and 1999. Non-cash investing activities include the acquisition of the remaining interest in Greenwald Intellicard for shares of common stock and options valued at \$696,000 in 2000.

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

#### THREE MONTHS ENDED MARCH 31, 2001 AND 2000

Management's Discussion and Analysis of Financial Condition and Results of Operations and other sections of this Form 10-Q contains forward-looking statements, including (without limitation) statements concerning possible or assumed future results of operations of PublicARD preceded by, followed by or that include the words "believes," "expects," "anticipates," "estimates," "intends," "plans" or similar expressions. For those statements, we claim the protection of the safe harbor for forward-looking statements contained in the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions. You should understand that such statements made under "Factors That May Affect Future Results" and elsewhere in this document could affect our future results and could cause those results to differ materially from those expressed in such forward-looking statements.

#### OVERVIEW

PublicARD, through its Infeiner subsidiaries, is a smart card technology company, which provides infrastructure products and solutions to facilitate secure access and transactions. The Company's products and solutions include integrated circuits, smart card readers and software systems. PublicARD sells its products and solutions to customers for deployment in enterprise and on-line security and transactions management applications. In May of 2000, PublicARD

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unveiled its new corporate brand of Infineer bringing together its subsidiaries located in Northern Ireland and the United States under a single focus in an effort to capitalize on its core competencies and growth opportunities in smart card technology.

PubliCARD established its presence within the smart card industry through a series of acquisitions:

- In February 1998, PubliCARD acquired, through a joint venture arrangement in Greenwald Intellicard, the assets and intellectual property of Intellicard Systems, Ltd. Greenwald Intellicard provides smart cards, smart card readers, value transfer stations, card management software and machine interface boards for the commercial laundry appliance industry. PubliCARD initially owned 50% of Greenwald Intellicard, and acquired the remaining 50% in February 1999 and February 2000.
- In November 1998, PubliCARD acquired Tritheim, which develops conditional access and security products for the software industry, computers and the electronic information and digital video broadcast, also known as DVB, industry.
- In February 1999, PubliCARD acquired Amazing, a developer of consumer smart card solutions and a manufacturer of customized smart cards.
- In February 1999, PubliCARD acquired Greystone, a developer of hard disk duplicators.
- In November 1999, PubliCARD acquired Absec, a designer of closed environment solutions, including small value electronic cash systems and database management solutions. Through Absec, PubliCARD provides systems for closed populations to allow individual user access, unique rights and monitoring.

While PubliCARD developed a number of successful smart card products and solutions, its operations were fragmented throughout a variety of markets. PubliCARD's Board of Directors, together

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with its management team, determined to integrate its operations and focus on a single market in which:

- high growth potential exists;
- PubliCARD has established relationships;
- PubliCARD has already deployed products and gained credibility; and
- PubliCARD possesses core technologies and competencies.

PubliCARD determined that it could leverage its existing smart card technology for deployment in the rapidly growing enterprise and on-line security, and transaction management market sectors, which PubliCARD had already penetrated and which it believed exhibited each of the characteristics identified above. To effect this new business strategy, in March 2000, the Company's Board of Directors adopted a plan to dispose of the operations of the Company's Greenwald, Greenwald Intellicard, Greystone and Amazing subsidiaries. These subsidiaries design, manufacture and distribute mechanical and smart card laundry solutions, hard disk duplicators and smart cards.

On June 29, 2000, the Company completed the sale of substantially

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all of the assets of Greenwald and Greenwald Intellicard to Eastern for \$22.5 million in cash less \$1.75 million held in escrow to secure the payment of certain indemnification obligations. As part of the transaction, Eastern assumed certain liabilities of Greenwald and Greenwald Intellicard, including certain contractual liabilities, accounts payable and accrued liabilities. The Company has substantially completed the wind-down of the operations of Amazing and Greystone including the sale of certain assets and the licensing of certain intellectual property.

In December 2000, the Company acquired a 3.5% ownership interest in TecSec for \$5.0 million. TecSec, a Virginia corporation, develops and markets smart card-based encryption products and solutions, which will enable the next generation information security for the enterprise, multi-enterprise e-business and other markets.

### Presentation

The results of operations for the three years ended December 31, 2000 reflect Greenwald, Greenwald Intellicard, Amazing and Greystone as discontinued operations. In addition, the results of operations for Tritheim and Absec have been reflected in the financial statements from their respective acquisition dates.

### Sales

Revenues are generated from infrastructure product sales, licenses of software products, maintenance contracts and software development services. Revenue from product sales is recorded upon shipment of the product. Provisions are recorded for estimated warranty repairs, returns and bad debts at the time the product is shipped. Software license fees are recognized upon shipment if a signed contract exists, the fee is fixed and determinable and the collection of the resulting receivable is probable. Revenue from maintenance and support fees are recognized ratably over the contract period.

### Cost of sales and operating expenses

Cost of sales consists primarily of third-party contract manufacturing costs, material, personnel costs and overhead.

Sales and marketing expenses consist primarily of personnel and travel costs, public relations, trade

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shows and marketing materials.

Product development expenses consist primarily of personnel and travel costs, independent consultants and contract engineering services. The Company believes that a significant level of development expenditures are required to enable it to quickly introduce new solutions that incorporate the latest technological advances and to develop and maintain close relationships with key suppliers of components and technologies. The Company's future success will depend upon its ability to develop and to introduce new solutions on a timely basis that keep pace with technological developments and emerging industry standards and address the increasingly sophisticated needs of its customers.

General and administrative expenses consist primarily of personnel and related costs for general corporate functions, including finance and accounting, human resources, risk management and legal.

### RESULTS OF OPERATIONS

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THREE MONTHS ENDED MARCH 31, 2001 COMPARED TO THREE MONTHS ENDED MARCH 31, 2000

**SALES.** Consolidated net sales decreased slightly to \$1.5 million in 2001 compared to \$1.6 million for 2000. The decrease in the first quarter sales is primarily attributed to lower closed environment solution sales in Europe offset by increased shipments of smart card readers for security applications.

**GROSS MARGIN.** Gross margin as a percentage of net sales decreased to 45% in 2001 from 52% in 2000. The decrease is attributed to the a percentage of sales derived from smart card reader solutions which generally command a lower gross margin than closed environment solutions.

**SALES AND MARKETING EXPENSES.** Sales and marketing expenses were \$1.3 million in 2001 compared to \$1.8 million in 2000. The decrease is mainly due to headcount reductions throughout 2000 and 2001 and lower consulting expenses for market research and corporate branding.

**PRODUCT DEVELOPMENT EXPENSES.** Product development expenses include expenses associated with the development of new products and enhancements to existing products. Product development expenses amounted to \$922,000 in 2001 compared to \$802,000 in 2000. Expenses increased in 2001 primarily due to contract engineering services for the ongoing integrated circuits, reader and software solution development efforts.

**GENERAL AND ADMINISTRATIVE EXPENSES.** General and administrative expenses for the quarter ended March 31, 2001 decreased by approximately 27% to \$1.3 million from \$1.8 million for 2000. The decrease was due to lower corporate expenditures, which consisted primarily of legal, consulting and professional fees, and headcount reductions.

**STOCK COMPENSATION EXPENSE.** Stock-based compensation recorded in 2000 and 2001 principally related to the change in terms of stock options awarded to two former employees of the Company and the issuance of stock awards and below market stock option grants to two executives hired in 1999.

**GOODWILL AMORTIZATION.** Goodwill and other intangibles associated with the Tritheim and Absec acquisitions are being amortized over a five-year period. Amortization amounted to \$660,000 in 2001 and 2000.

**OTHER INCOME AND EXPENSE.** Interest income increased slightly to \$207,000 for 2001 from \$188,000 for 2000 principally due to higher cash balances. Interest expense, which principally relates to interest on the remaining environmental obligation (see below), decreased to \$19,000 in 2001 compared to \$38,000 in 2000.

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LIQUIDITY

The Company has financed its operations over the last two years primarily through the sale of common and preferred stock and the sale of non-core businesses. During the quarter ended March 31, 2001, cash, including short-term investments, decreased by \$3.9 million to \$13.1 million as of March 31, 2001.

Operating activities from continuing operations utilized cash of \$3.9 million for the three months ended March 31, 2001 and principally consisted of the loss from continuing operations of \$3.5 million and an increase in net operating assets and liabilities of \$1.2 million offset by non-cash charges of \$746,000 for goodwill amortization, stock compensation expense and depreciation. Operating activities from discontinued operations utilized \$91,000 of cash.

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Investing activities provided cash of \$137,000 in 2001 and consisted principally of proceeds from the sale of discontinued operations offset partially by capital expenditures and closing costs associated with the Company's December 2000 investment in TecSec.

Financing activities utilized cash of \$35,000 in 2001 and consisted of closing costs in connection with the Company's December 2000 private placement of common and preferred stock. The effect of exchange rate changes on cash and cash equivalents reduced cash by \$5,000.

During the first quarter of 2001, the Company's capital expenditures from continuing operations totaled \$34,000. The Company anticipates that its level of capital expenditures for 2001 will approximate the prior year. The Company has not entered into any material commitments for acquisitions or capital expenditures and has the ability to increase or decrease capital expenditure levels as required. The Company anticipates that it will be able to fund its capital expenditures during 2001 with its available cash resources.

The Company has experienced negative cash flow from operating activities in the past and expects to experience negative cash flow in 2001 and 2002. Future uses of cash include the following:

- The Company will incur expenditures to support the expansion of sales and marketing efforts, new product development, working capital growth and capital expenditures. Also, there will be a need to fund new initiatives in the smart card market before there is a reasonable expectation to derive any significant revenues from this market.
- In April 1996, a consent decree (the "Consent Decree") among the Company, the United States Environmental Protection Agency and the Pennsylvania Department of Environmental Protection ("PADEP") was entered by the court which resolved all of the United States' and PADEP's claims against the Company for recovery of costs incurred in responding to releases of hazardous substances at a facility previously owned and operated by the Company. Pursuant to the Consent Decree, the Company will pay a total of \$14.4 million plus interest to the United States and Commonwealth of Pennsylvania. Through March 31, 2001, the Company has made principal payments aggregating \$12.8 million. Further payments totaling \$1.7 million, including interest, will be made to the United States Environmental Protection Agency in the amounts of \$862,000 due April 2001 and \$823,000 due April 2002.
- The Company sponsors a defined benefit pension plan, which was frozen in 1993. As of December 31, 2000, the actuarial present value of accrued liabilities exceeded the plan assets by approximately \$5.4 million. The annual contribution to the plan is expected to be approximately \$1.2 million in 2001 and beyond.

The Company believes that its current cash balance and expected cash flows will satisfy working capital, new product development, sales and marketing expansion and capital expenditures for at least the

next 12 months. However, if during this period or thereafter, the Company is not successful in generating sufficient cash flow from operations or in raising additional capital when required in sufficient amounts and on terms acceptable to the Company or at all, the Company may be required to scale back the scope of

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its business plan, which would have a material adverse effect on the Company's financial condition or results of operations. The Company cannot make any assurances that it will generate sufficient cash flow from operations in the future, that anticipated revenue growth will be realized or that future borrowings or equity contributions will be available in amounts sufficient to finance the Company's business plan or at all.

As of March 31, 2001, the value of the Company's investment in TecSec, a privately held company, was \$5.0 million. This investment has been accounted for at cost and could be subject to write-down in future periods if it is determined that the investment is permanently impaired and not recoverable. TecSec is currently evaluating alternative sources of financing to meet ongoing capital and operating needs. If TecSec is not successful in obtaining sufficient capital on acceptable terms or at all, the Company's investment in TecSec could be permanently impaired and subject to a significant write-down.

As of December 31, 2000, approximately \$96 million of U.S. tax loss carryforwards (subject to review by the Internal Revenue Service), expiring from 2001 through 2020, were available to offset future taxable income. Due to the "change of ownership" provisions of the Internal Revenue Code of 1986, the availability of net operating loss carryforwards to offset federal taxable income in future periods could be subject to an annual limitation if a change in ownership for income tax purposes occurs.

### FACTORS THAT MAY AFFECT FUTURE RESULTS

WE HAVE A HISTORY OF OPERATING LOSSES AND NEGATIVE CASH FLOW, AND WE HAVE ONGOING FUNDING OBLIGATIONS. We have incurred losses and experienced negative cash flow from operating activities in the past, and we expect to incur losses and experience negative cash flow from operating activities in the foreseeable future. We incurred losses from continuing operations in 1998, 1999, 2000 and for the three months ended March 31, 2001, of approximately \$8.4 million, \$16.7 million, \$19.7 million and \$3.5 million, respectively. In addition, we experienced negative cash flow from continuing operating activities of \$5.6 million, \$8.5 million, \$18.7 million and \$3.9 million in 1998, 1999, 2000 and for the three months ended March 31, 2001, respectively.

We expect that our businesses will require on-going funding to support the expansion of sales and marketing efforts, new product development, working capital growth and capital expenditures. Also, we will need to fund our new initiatives in the broadband market before we can reasonably expect to derive any significant revenues from this market.

We also have continuing obligations to fund payments due under the Consent Decree and an underfunded pension plan. As of March 31, 2001, we were required to make future aggregate payments of \$1.7 million through April 2002 in connection with the Consent Decree. Consistent with the general practices of environmental enforcement agencies, the Consent Decree does not eliminate our potential liability for remediation of contamination that had not been known at the time of the settlement. We sponsor a defined benefit pension plan, which was frozen in 1993. As of December 31, 2000, the present value of the accrued benefit liabilities of our pension plan exceeded the plan's assets by approximately \$5.4 million. In addition to the \$1.2 million we expect to contribute to the plan in 2001, we are obligated to make continued contributions to the plan in accordance with the rules and regulations prescribed by the Employee Retirement Income Security Act of 1974. Future contribution levels depend in large measure on the mortality rate of plan participants and the investment return on the plan assets.

WE HAVE LIMITED EXPERIENCE IN THE SMART CARD MARKET. We have only recently begun to provide smart card infrastructure products and solutions which facilitate secure access and transactions. We are therefore subject to the risks

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inherent in establishing a new business enterprise.

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Our business model is new and unproven and may not generate sufficient revenue for us to be successful. The volume of products and services distributed using our technology may be too small to support or grow our business.

OUR FUTURE PROFITABILITY DEPENDS LARGELY UPON PRODUCTS AND FUTURE PRODUCTS THAT HAVE NOT YET PRODUCED ANY REVENUES OR ARE NOT YET COMMERCIALY VIABLE. We believe that certain of our products are viable, but have not yet generated any material sales. Our future revenues and earnings depend in large part on the success of these products. Our business is also based on products not yet developed. There are no assurances that these products will be developed into working products or that a market will develop for these products in the future.

THE MARKET'S ACCEPTANCE OF OUR PRODUCTS IS UNCERTAIN. Demand for, and market acceptance of, our smart card reader, application specific integrated circuits ("ASICs") and software solutions are subject to a high level of uncertainty due to rapidly changing technology, new product introductions and changes in customer requirements and preferences. The success of our products or any future products also depends upon our ability to enhance our existing products and to develop and introduce new products and technologies to meet customer requirements. We face the risk that our current and future products will not achieve market acceptance.

Our solutions are designed to provide secure electronic commerce, access control and security for various digital platforms. The markets for secure access and transaction management applications are still emerging, and if the benefits are not perceived sufficient or if alternative technologies are more widely accepted, then the demand for our solutions may not grow and our business and operating results would be materially and adversely affected.

WE DEPEND ON A RELATIVELY SMALL NUMBER OF CUSTOMERS FOR A MAJORITY OF OUR REVENUES. We rely on a limited number of customers in our business. We expect to continue to depend upon a relatively small number of customers for a majority of the revenues in our business. For the three months ended March 31, 2001, two customers represented approximately 22% of our net sales and no customer represented more than 10% of our accounts receivable balance as of March 31, 2001.

We generally do not enter into long-term supply commitments with our customers. Instead, we bid on a project basis and have supply contracts in place for each project. Significant reductions in sales to any of our largest customers would have a material adverse effect on our business. In addition, we generate significant accounts receivable and inventory balances in connection with providing products to our customers. A customer's inability to pay for our products could have a material adverse effect on our results of operations.

WE DEPEND ON THIRD PARTY MANUFACTURERS WHO ARE OUTSIDE OF OUR CONTROL. We outsource manufacturing needs of a significant portion of our products to third party contract manufacturers. Outsourcing of manufacturing involves risks with respect to quality assurance, cost and the absence of engineering support. In addition, financial, operational or supply problems encountered by the third party manufacturers we use or may use in the future, their subcontractors or their suppliers could result in our inability to obtain timely delivery, if at all, of finished products. Any such difficulties would adversely affect our financial results.

WE HAVE A LIMITED NUMBER OF SUPPLIERS OF KEY COMPONENTS. We rely on a limited number of suppliers for key components for our products. For example, we



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purchase embedded chips for ASICs exclusively from the Atmel Corporation. Our reliance on one supplier could impose several risks, including an inadequate supply of chips, price increases, long lead times, late deliveries and poor quality. Disruption or termination of the supply of these chips could delay the delivery of our products, which could have a

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material adverse effect on our business and operating results. These delays could damage our relationship with current and prospective customers.

OUR FUTURE SUCCESS DEPENDS ON OUR ABILITY TO KEEP PACE WITH TECHNOLOGICAL CHANGES AND INTRODUCE NEW PRODUCTS IN A TIMELY MANNER. The rate of technological change currently affecting the smart card market is particularly rapid compared to other industries. Our ability to anticipate these trends and adapt to new technologies is critical to our success. Because new product development commitments must be made well in advance of actual sales, new product decisions must anticipate future demand as well as the speed and direction of technological change. Our ability to remain competitive will depend upon our ability to develop in a timely and cost effective manner new and enhanced products at competitive prices. New product introductions or enhancements by our competitors could cause a decline in sales or loss of market acceptance of our existing products and lower profit margins.

Our success in developing, introducing and selling new and enhanced products depends upon a variety of factors, including:

- product selections;
- timely and efficient completion of product design and development;
- timely and efficient implementation of manufacturing processes;
- effective sales, service and marketing;
- price; and
- product performance in the field.

Our ability to develop new products also depends upon the success of our research and development efforts. Our research and development expenditures for the three months ended March 31, 2001 were \$922,000 and we may need to devote substantially more resources to our research and development efforts in the future. We cannot assure you that these expenditures will lead to the development of viable products.

THE HIGHLY COMPETITIVE MARKETS IN WHICH WE OPERATE COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS AND OPERATING RESULTS. The markets in which we operate are intensely competitive and characterized by rapidly changing technology. We compete against numerous companies, many of which have greater resources than we do, and we believe that competition is likely to intensify.

We believe that the principal competitive factors affecting us are:

- the extent to which products support industry standards and are capable of being operated or integrated with other products;
- technical features and level of security;
- strength of distribution channels;

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- price;
- product reputation, reliability, quality, performance and customer support;
- product features such as adaptability, functionality and ease of use; and

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- competitor reputation, positioning and resources.

We cannot assure you that competitive pressures will not have a material adverse effect on our business and operating results. Many of our current and potential competitors have longer operating histories and significantly greater financial, technical, sales, customer support, marketing and other resources, as well as greater name recognition and a larger installed base of their products and technologies than our company. Additionally, there can be no assurance that new competitors will not enter our markets. Increased competition would likely result in price reductions, reduced margins and loss of market share, any of which would have a material adverse effect on our business and operating results.

The market for smart card products and solutions is new, intensely competitive and rapidly evolving. We expect competition to continue to increase with both our existing competitors and new market entrants. Our primary competition currently comes from or is anticipated to come from:

- companies offering payment solutions, including Trintech and VeriFone;
- companies offering smart card technology solutions, including Gemplus, Philips and SCM Microsystems; and
- companies offering closed environment solutions, including small value electronic cash systems and database management solutions, such as Girovend, MARS, Diebold, CyberMark and Schlumberger.

Many of our current and potential competitors have broader customer relationships that could be leveraged, including relationships with many of our customers. These companies also have more established customer support and professional services organizations than we do. In addition, a number of companies with significantly greater resources than we have could attempt to increase their presence by acquiring or forming strategic alliances with our competitors, resulting in increased competition.

OUR LONG PRODUCT SALES CYCLES SUBJECT US TO RISK. Our products fall into two categories, those that are standardized and ready to install and use and those that require significant development efforts to implement within the purchasers' own systems. Those products requiring significant development efforts tend to be newly developed technologies and software applications that can represent major investments for customers. We rely on potential customers' internal review processes and systems requirements. The implementation of some of our products involves deliveries of small quantities for pilot programs and significant testing by the customers before firm orders are received for production volumes, or lengthy beta testing of software solutions. For these more complex products, the sales process may take one year or longer, during which time we may expend significant financial, technical and management resources, without any certainty of a sale.

WE MAY BE LIMITED IN OUR USE OF OUR FEDERAL NET OPERATING LOSS CARRYFORWARDS. As of December 31, 2000, we had federal net operating loss

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carryforwards, subject to review by the Internal Revenue Service, totaling approximately \$96.0 million for federal income tax purposes, approximately \$9.0 million of which will expire at the end of 2001 and \$25.0 million of which will expire at the end of 2002. We do not expect to earn any significant taxable income prior to 2003, and may not do so until later. A federal net operating loss can generally be carried back two or three years and then forward fifteen or twenty years (depending on the year in which the loss was incurred), and used to offset taxable income earned by a company (and thus reduce its income tax liability).

Section 382 of the Internal Revenue Code provides that when a company undergoes an "ownership change," that company's use of its net operating losses is limited in each subsequent year. An

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"ownership change" occurs when, as of any testing date, the sum of the increases in ownership of each shareholder that owns five percent or more of the value of a company's stock as compared to that shareholder's lowest percentage ownership during the preceding three-year period exceeds fifty percentage points. For purposes of this rule, certain shareholders who own less than five percent of a company's stock are aggregated and treated as a single five-percent shareholder. We may issue a substantial number of shares of our stock in connection with public and private offerings in the future. In addition, the exercise of outstanding warrants and options to purchase shares of our common stock may require us to issue additional shares of our common stock. The issuance of a significant number of shares of stock could result in an "ownership change." If we were to experience such an "ownership change," we estimate that we would not be able to use a substantial amount of our available federal net operating loss carryforwards to reduce our taxable income.

The extent of the actual future use of our federal net operating loss carryforwards is subject to inherent uncertainty because it depends on the amount of otherwise taxable income we may earn. We cannot give any assurance that we will have sufficient taxable income in future years to use any of our federal net operating loss carryforwards before they would otherwise expire.

OUR PROPRIETARY TECHNOLOGY IS DIFFICULT TO PROTECT AND MAY INFRINGE ON THE INTELLECTUAL PROPERTY RIGHTS OF THIRD PARTIES. Our success depends significantly upon our proprietary technology. We rely on a combination of patent, copyright and trademark laws, trade secrets, confidentiality agreements and contractual provisions to protect our proprietary rights. We seek to protect our software, documentation and other written materials under trade secret and copyright laws, which afford only limited protection. We currently have a number of patent applications pending. We cannot assure you that any of our applications will be approved, that any new patents will be issued, that we will develop proprietary products or technologies that are patentable, that any issued patent will provide us with any competitive advantages or will not be challenged by third parties. Furthermore, we cannot assure you that the patents of others will not have a material adverse effect on our business and operating results.

If our technology or products is determined to infringe upon the rights of others, and we were unable to obtain licenses to use the technology, we could be required to cease using the technology and stop selling the products. We may not be able to obtain a license in a timely manner on acceptable terms or at all. Any of these events would have a material adverse effect on our financial condition and results of operations.

Patent disputes are common in technology related industries. We cannot assure you that we will have the financial resources to enforce or defend a patent infringement or proprietary rights action. As the number of products and

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competitors in the smart card market grows, the likelihood of infringement claims also increases. Any claim or litigation may be time consuming and costly, cause product shipment delays or require us to redesign our products or enter into royalty or licensing agreements. Any of these events would have a material adverse effect on our business and operating results. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or to use our proprietary information and software. In addition, the laws of some foreign countries do not protect proprietary and intellectual property rights to as great an extent as do the laws of the United States. Our means of protecting our proprietary and intellectual property rights may not be adequate. There is a risk that our competitors will independently develop similar technology, duplicate our products or design around patents or other intellectual property rights.

IF THIRD PARTIES DO NOT DEPLOY OUR TECHNOLOGY AND CREATE A MARKET FOR DIGITAL COMMERCE, OUR BUSINESS WILL BE HARMED. Relationships with leading content, technology and commerce service providers are critical to our success. Our business and operating results would be harmed to the extent our strategic partnerships fail, in whole or in part, to:

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- deploy our technology;
- develop an infrastructure to conduct business through e-commerce;  
and
- develop and deploy new applications.

THE NATURE OF OUR PRODUCTS SUBJECTS US TO PRODUCT LIABILITY RISKS. Our customers may rely on certain of our current products and products in development to prevent unauthorized access to digital content, computer networks, DVB and real property. A malfunction of or design defect in certain of our products could result in tort or warranty claims. Although we attempt to reduce the risk of exposure from such claims through warranty disclaimers and liability limitation clauses in our sales agreements and by maintaining product liability insurance, we cannot assure you that these measures will be effective in limiting our liability for any damages. Any liability for damages resulting from security breaches could be substantial and could have a material adverse effect on our business and operating results. In addition, a well-publicized actual or perceived security breach involving our conditional access or security products could adversely affect the market's perception of our products in general, regardless of whether any breach is attributable to our products. This could result in a decline in demand for our products, which would have a material adverse effect on our business and operating results.

WE MAY HAVE DIFFICULTY RETAINING OR RECRUITING PROFESSIONALS FOR OUR BUSINESS. Our future success and performance is dependent on the continued services and performance of our senior management and other key personnel. There is a shortage of qualified marketing and technical personnel in our industry, and the competition for such personnel is intense. Accordingly, the loss of the services of any of our executive officers or other key employees could materially adversely affect our business.

Our business requires experienced software programmers, creative designers and application developers, and our success depends on identifying, hiring, training and retaining such experienced, knowledgeable professionals. If a significant number of our current employees or any of our senior technical personnel resign, or for other reasons are no longer employed by us, we may be unable to complete or retain existing projects or bid for new projects of similar scope and revenues. In addition, former employees may compete with us in

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the future.

Even if we retain our current employees, our management must continually recruit talented professionals in order for our business to grow. There is currently a shortage of qualified senior technical personnel in the software development field, and this shortage is likely to continue. Furthermore, there is significant competition for employees with the skills required to perform the services we offer. We cannot assure you that we will be able to attract a sufficient number of qualified employees in the future to sustain and grow our business, or that we will be successful in motivating and retaining the employees we are able to attract. If we cannot attract, motivate and retain qualified professionals, our business, financial condition and results of operations will suffer.

OUR INTERNATIONAL OPERATIONS SUBJECT US TO RISK ASSOCIATED WITH OPERATING IN FOREIGN MARKETS, INCLUDING FLUCTUATIONS IN CURRENCY EXCHANGE RATES, WHICH COULD ADVERSELY AFFECT OUR OPERATIONS AND FINANCIAL CONDITION. International sales represented approximately 58% of total sales for the three months ended March 31, 2001. Because we derive a substantial portion of our business outside the United States, we are subject to certain risks associated with operating in foreign markets including the following:

- tariffs and other trade barriers;
- difficulties in staffing and managing foreign operations;
- currency exchange risks;

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- export controls related to encryption technology;
- unexpected changes in regulatory requirements;
- changes in economic and political conditions;
- potentially adverse tax consequences; and
- burdens of complying with a variety of foreign laws.

Any of the foregoing could adversely impact the success of our international operations. We cannot assure you that such factors will not have a material adverse effect on our future international sales and, consequently, on our business, operating results and financial condition. In addition, fluctuations in exchange rates could have a material adverse effect on our business, operating results and financial condition. To date, we have not engaged in currency hedging.

OUR ARTICLES OF INCORPORATION AND BY-LAWS, CERTAIN CHANGE OF CONTROL AGREEMENTS, OUR RIGHTS PLAN AND PROVISIONS OF PENNSYLVANIA LAW COULD DETER TAKEOVER ATTEMPTS.

Blank check preferred stock. Our board of directors has the authority to issue preferred stock and to fix the rights, preferences, privileges and restrictions, including voting rights, of these shares without any further vote or action by the holders of our common stock. The rights of the holders of any preferred stock that may be issued in the future may adversely affect the rights of the holders of our common stock. The issuance of preferred stock could make it more difficult for a third party to acquire a majority of our outstanding voting stock, thereby delaying, deferring or preventing a change of control.

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Such preferred stock may have other rights, including economic rights, senior to our common stock, and as a result, the issuance of the preferred stock could limit the price that investors might be willing to pay in the future for shares of our common stock and could have a material adverse effect on the market value of our common stock.

Rights plan. Our rights plan entitles the registered holders of rights to purchase shares of our class A preferred stock upon the occurrence of certain events, and may have the effect of delaying, deferring or preventing a change of control.

Change of control agreements. We are a party to change of control agreements which provide for payments to certain of our directors and executive officers under certain circumstances following a change of control. Since the change of control agreements require large cash payments to be made by any person effecting a change of control, these agreements may discourage takeover attempts.

The change of control agreements provide that, if the services of any person party to a change of control agreement are terminated within three years following a change of control, that individual will be entitled to receive, in a lump sum within 10 days of the termination date, a payment equal to 2.99 times that individual's average annual compensation for the shorter of the five years preceding the change of control and the period the individual received compensation from us for personal services. Assuming a change of control were to occur at the present time, payments in the following amounts would be required: Mr. Harry I. Freund -- \$964,000; and Mr. Jay S. Goldsmith -- \$964,000. If any such payment, either alone or together with others made in connection with the individual's termination, is considered to be an excess parachute payment under the Internal Revenue Code, the individual will be entitled to receive an additional payment in an amount which, when added to the initial payment, would result in a net benefit to the individual, after giving effect to excise taxes imposed by Section 4999 of the Internal Revenue Code and

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income taxes on such additional payment, equal to the initial payment before such additional payment. We would not be able to deduct these payments for income tax purposes.

Pennsylvania law. We are a Pennsylvania corporation. Anti-takeover provisions of Pennsylvania law could make it difficult for a third party to acquire control of us, even if such change of control would be beneficial to our shareholders.

OUR STOCK PRICE IS EXTREMELY VOLATILE. The stock market has recently experienced significant price and volume fluctuations unrelated to the operating performance of particular companies. The market price of our common stock has been highly volatile and is likely to continue to be volatile. The future trading price for our common stock will depend on a number of factors, including:

- variations in our annual or quarterly financial results or those of our competitors;
- general economic conditions, in particular, the technology service sector;
- the volume of activity for our common stock is minimal and therefore a large number of shares placed for sale or purchase could increase its volatility;

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- our ability to effectively manage our business;
- expected or announced relationships with other companies;
- announcements of technological advances innovations or new products by us or our competitors;
- patents or other proprietary rights or patent litigation; and
- product liability or warranty litigation.

We cannot be certain that the market price of our common stock will not experience significant fluctuations in the future, including fluctuations that are adverse and unrelated to our performance.

WE ARE SUBJECT TO GOVERNMENT REGULATION. The telecommunications, media, broadcast and cable television industries are subject to extensive regulation by governmental agencies. These governmental agencies continue to oversee and adopt legislation and regulation over these industries, which may affect our business, market participants with which we have relationships or the acceptance of interactive television in general. In addition, future legislation or regulatory requirements regarding privacy issues could be enacted to require notification to users that captured data may be used by marketing entities to target product promotion and advertising to that user. Any of these developments may materially adversely affect our business.

Federal, state and local regulations impose various environmental controls on the discharge of chemicals and gases, which may be used in our present or future assembly processes. Moreover, changes in such environmental rules and regulations may require us to invest in capital equipment and implement compliance programs in the future. Any failure by us to comply with environmental rules and regulations, including the discharge of hazardous substances, would subject us to liabilities and would materially adversely affect our operations.

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### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### Foreign currency exchange rate risk

We conduct operations in the United Kingdom and sell products in several different countries. Therefore, our operating results may be impacted by the fluctuating exchange rates of foreign currencies, especially the British pound, in relation to the U.S. dollar. We do not currently engage in hedging activities with respect to our foreign currency exposure. We continually monitor our exposure to currency fluctuations and may use financial hedging techniques when appropriate to minimize the effect of these fluctuations. Even so, exchange rate fluctuations may still have a material adverse effect on our business and operating results.

#### Market Risk

We are exposed to market risk primarily through short-term investments. Our investment policy calls for investment in short-term, low risk instruments. As of March 31, 2001, short-term investments (principally U.S. Treasury bills) were \$12.9 million. Due to the nature of these investments, any decrease in rates would not have a material impact on our financial condition or results of operations.

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### Investment Risk

As of March 31, 2001, the value of our investment in TecSec, a privately held company, was \$5.0 million. This investment has been accounted for at cost and could be subject to write-down in future periods if it is determined that the investment is permanently impaired and not recoverable. TecSec is currently evaluating alternative sources of financing to meet ongoing capital and operating needs. If TecSec is not successful in obtaining sufficient capital on acceptable terms or at all, our investment in TecSec could be permanently impaired and subject to a significant write-down.

### PART II. OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

##### GENERAL LITIGATION

Various legal proceedings are pending against the Company. The Company considers all such proceedings to be ordinary litigation incident to the character of its business. Certain claims are covered by liability insurance. The Company believes that the resolution of those claims to the extent not covered by insurance will not, individually or in the aggregate, have a material adverse effect on the financial position or results of operations of the Company.

#### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

None.

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#### 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.

PUBLICARD, INC.  
(Registrant)

Date: May 11, 2001

/s/ Jan-Erik Rottinghuis  
Jan-Erik Rottinghuis, President  
and Chief Executive Officer

/s/ Antonio L. DeLise  
Antonio L. DeLise, Chief Financial  
Officer, Secretary and Principal  
Accounting Officer

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