

Edgar Filing: PUBLICARD INC - Form 10-K

PUBLICARD INC  
Form 10-K  
March 31, 2003

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K  
-----

(Mark One)

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2002

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 23-0991870  
(State or other jurisdiction of (I.R.S. Employer Identification No.)  
incorporation or organization)

620 FIFTH AVENUE, 7TH FLOOR, NEW YORK, NY 10020  
(Address of principal executive offices) (Zip code)

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

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class -----	Name of each exchange on which registered -----
NONE	NONE

Securities Registered Pursuant To Section 12(g) of the Act  
COMMON STOCK (\$.10 PAR VALUE)  
RIGHTS TO PURCHASE CLASS A PREFERRED STOCK, FIRST SERIES

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

AS OF JUNE 28, 2002, THE AGGREGATE MARKET VALUE OF THE VOTING COMMON STOCK HELD

## Edgar Filing: PUBLICARD INC - Form 10-K

BY NON-AFFILIATES OF THE REGISTRANT WAS APPROXIMATELY \$3,890,000.

NUMBER OF SHARES OF COMMON STOCK OUTSTANDING AS OF MARCH 24, 2003: 24,440,902

### Documents Incorporated By Reference

PART III, ITEMS 10, 11, 12 AND 13, ARE INCORPORATED BY REFERENCE FROM THE REGISTRANT'S DEFINITIVE PROXY STATEMENT TO BE FILED PURSUANT TO REGULATION 14A FOR THE 2003 ANNUAL MEETING OF SHAREHOLDERS.

### PART I

This Form 10-K contains forward-looking statements, including (without limitation) statements concerning possible or assumed future results of operations of PublicARD, Inc. and subsidiaries, ("PublicARD" or the "Company") 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.

#### ITEM 1. BUSINESS

PublicARD, through its Infineer Ltd. subsidiary, is a smart card technology company, which designs and develops smart card software and hardware solutions for campus environments. This market includes institutions such as corporate campuses, secondary schools and universities. The Company's ChipNet solution focuses on delivering a multi-functional platform to control access to and payment for a wide variety of applications using a single smart card. The solution has been designed to accommodate integration with a range of third party technologies. The Company believes that the educational, government and corporate sectors all continue to move toward the more functional and broader applications that a smart card solution can provide over traditional methods. The Company sells its transaction solutions to value-added resellers and distributors, and directly to end-users.

At present, PublicARD's sole operating activities are conducted through its Infineer Ltd. subsidiary. The Company's future plans revolve around a potential acquisition strategy that would focus on businesses in areas outside the high technology sector while continuing to support the expansion of the Infineer business. However, the Company will not be able to implement such plans unless it is successful in obtaining funding, as to which no assurance can be given.

The consolidated financial statements included in this Form 10-K contemplate the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred operating losses, a substantial decline in working capital and negative cash flow from operations for the years 2002, 2001 and 2000. The Company has also experienced a substantial reduction in its cash and short term investments, which declined from \$17.0 million at December 31, 2000, to \$4.5 million at December 31, 2001 and to \$1.3 million at December 31, 2002. The Company also had a working capital deficiency of \$548,000 and an accumulated deficit of \$112.0 million at December 31, 2002.

If the distress termination of the Company's defined benefit pension plan for which the Company has applied is completed (see Note 5 to the Notes to

## Edgar Filing: PUBLICARD INC - Form 10-K

Consolidated Financial Statements), the Company's 2003 funding requirements to the plan could be eliminated, in which case management believes that existing cash and short term investments may be sufficient to meet the Company's operating and capital requirements at the currently anticipated levels through December 31, 2003. However, additional capital will be necessary in order to operate beyond December 2003 and to fund the current business plan and other obligations. While the Company is actively considering various funding alternatives, the Company has not secured or entered into any arrangements to obtain additional funds. There can be no assurance that the Company will eliminate the 2003 funding requirements for the defined benefit pension plan or be able to obtain additional funding on acceptable terms or at all. If the Company cannot raise additional capital to continue its present level of operations it may not be able to meet its obligations, take advantage of future acquisition opportunities or further develop or enhance its product offering, any of which could have a material adverse effect on its business and results of operations and could lead the Company to seek bankruptcy protection. These conditions raise substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the Company's failure to obtain funding or inability to continue as a going concern.

1

### INDUSTRY

Security and privacy are primary concerns of the ever-growing information economy. The expected level of growth in secure business-to-business and consumer-to-business transactions will only occur if consumers, businesses, governments and other organizations are confident that their network and Internet exchanges and transactions are secure from unauthorized intrusion, usage, sabotage and theft. To effectively address the growing need for greater enterprise and on-line security, individuals and organizations are turning to smart card technology. Through its central processing and memory capabilities, smart card technology enables cryptographic communications, authentication and other applications that permit secure data access, information exchange and electronic transactions within network and Internet environments.

A smart card is similar in appearance to a traditional credit card, but unlike a traditional credit card, stores information on an integrated circuit chip embedded within the card, rather than on a magnetic stripe on the surface. While a typical magnetic stripe card stores approximately 212 bytes of information, generally consisting of a user's name, account and personal identification number, a smart card can store 64 kilobytes or more of information, which is 300 times that of a traditional magnetic stripe credit card. Additionally, the integrated circuit within a smart card serves as a central processing unit which, combined with its memory capacity, facilitates the use of encryption applications, which secure data and value exchanges within networks and the Internet. Smart cards also permit bi-directional authentication in which the smart card can authenticate the validity of the intended party or device prior to exchanging information or value.

The rollout of smart card technology started in the telecommunication sector, specifically to facilitate the use of public payphones (replacing coins) and mobile phones (Subscriber Identification Modules). Of the 2 billion smart cards issued in 2000, half of them were issued in this sector. The deployment of smart card technology in this sector demonstrates the security and adaptability of the technology and evidences that smart cards are a unique media to store, transport and process personal information, access keys and other information.

Smart card technology is now being widely deployed in other market

## Edgar Filing: PUBLICARD INC - Form 10-K

sectors, including the security and transaction management sectors. In the security sector, smart card technology is being used to authenticate and secure access to physical premises, PCs, networks, virtual private networks, and the Internet, and through cryptography, facilitate secure email, electronic document and information exchanges, e-commerce transactions/payments and other Internet and broadband applications. In the transaction management sector, smart card technology is being used within a variety of closed system environments. For example, smart card technology is being used in the banking sector to secure payment transactions in physical and virtual worlds and in the transportation sector to replace "tickets," thereby speeding up the ticketing process and making it more efficient. Other closed environments such as corporate or educational campuses are using smart card technology to resolve a mix of both security and transactions needs including purchase and payment transactions, identification, authentication and access.

Demand for smart card solutions are being further driven by governments and financial institutions. The U.S. Government Paperwork Elimination Act of 1995 requires that all federal agencies offer electronic exchange of mandatory data by October 2003. The European Commission ("EC") is also supporting the adoption of smart card technology in their continuing efforts to create a more efficient and competitive economy within the European community. Through the eEurope program, the EC is sponsoring programs to standardize smart card infrastructure devices and harmonize system platforms. Finally, smart card technology is rapidly becoming a key facilitator of financial transactions. The financial and banking community in Asia and Europe is using smart card technology to support credit, debit and e-purse cards (cards that store cash values), multi-application services and services dealing with coupons and/or tickets. Several large U.S. financial institutions, including American Express, MasterCard and Visa International, have introduced smart cards as part of their financial card systems.

The use of smart card technology is especially well suited for managing transactions in closed environment solutions that restrict access and manage payments. In closed environments, smart cards are

2

used to control access to physical premises, process payments and provide portable network security. The Company believes that the educational, government and corporate sectors all continue to provide growth opportunities as these institutions move toward the more functional and broader applications that a smart card solution can provide over other traditional methods. Smart card solutions offer a greater level of flexibility and permit development of customer specific applications that cannot be offered by traditional methods of providing closed environment security and transaction management such as the magnetic stripe.

With the increased use and acceptance of smart cards and the related technologies world wide, there are numerous applications to use smart card technology in a variety of infrastructure platforms. PubliCARD has developed a client-server based software solution for closed campus proprietary card users, which is focused on delivering multi-functionality around a single card supporting a wide range of third party technologies.

### STRATEGY

### HISTORY OF THE COMPANY'S SMART CARD INITIATIVE

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

## Edgar Filing: PUBLICARD INC - Form 10-K

- In February 1998, PubliCARD acquired, through a joint venture arrangement in Greenwald Intellicard, Inc. ("Greenwald Intellicard"), the assets and intellectual property of Intellicard Systems, Ltd. Greenwald Intellicard provided 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 Technologies, Inc. ("Tritheim"), which developed conditional access and security products for, computers and the electronic information and the digital video broadcast industry. In May 2000, the Company changed the name of its Tritheim subsidiary to Infineer, Inc. as part of a re-branding effort.
- In February 1999, PubliCARD acquired Amazing! Smart Card Technologies, Inc. ("Amazing"), a developer of consumer smart card solutions and a manufacturer of customized smart cards.
- In February 1999, PubliCARD acquired Greystone Peripherals, Inc. ("Greystone"), a developer of hard disk duplicators.
- In November 1999, PubliCARD acquired Absec Limited ("Absec"), a designer of closed environment solutions, including small value electronic cash systems and database management solutions. In May of 2000, the Company changed the name of its Absec subsidiary to Infineer Ltd. ("Infineer") as part of a re-branding effort.

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

- high growth potential existed;
- PubliCARD had established relationships;
- PubliCARD had already deployed products and gained credibility; and
- PubliCARD possessed core technologies and competencies.

PubliCARD believed 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

3

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 Industries Inc. ("Greenwald"), Greenwald Intellicard, Greystone and Amazing subsidiaries. These subsidiaries designed, manufactured and distributed mechanical and smart card laundry solutions, hard disk duplicators and smart cards.

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

## Edgar Filing: PUBLICARD INC - Form 10-K

transaction, Eastern assumed certain liabilities of Greenwald and Greenwald Intellicard, including certain contractual liabilities, accounts payable and accrued liabilities. The Company has 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 Incorporated ("TecSec") for \$5.1 million. TecSec, a Virginia company, develops and markets encryption products and solutions, which are designed to enable the next generation information security for the enterprise, multi-enterprise e-business and other markets.

In July 2001, after evaluating the timing of potential future revenues, PublicARD's Board decided to shift the Company's strategic focus. While the Board remained confident in the long-term prospects of the smart card business, the timing of public sector and corporate initiatives in wide-scale, broadband environments utilizing the Company's smart card reader and chip products had become more uncertain. Given the lengthened time horizon, the Board did not believe it would be prudent to continue to invest the Company's current resources in the ongoing development and marketing of these technologies. Accordingly, the Board determined that shareholders' interests will be best served by pursuing strategic alliances with one or more companies that have the resources to capitalize more fully on the Company's smart card reader and chip-related technologies. In connection with this shift in the Company's strategic focus, workforce reductions and other measures were implemented to achieve cost savings.

In September 2001, the Company formed a new minority-owned affiliate, Mako Technologies LLC ("Mako") to market its smart card reader and chip technologies. The move is consistent with the Company's decision to explore strategic transactions that would enable the Company to reduce or eliminate its ongoing cash funding requirements for its smart card reader and chip business while retaining an interest in the upside potential for these technologies. The Company contributed certain inventories and equipment valued at \$238,000, in exchange for a 31% fully diluted ownership interest in Mako. The Company also granted a license of its reader and chip technology to Mako in exchange for royalties based on sales over the next two years. After reducing headcount and reassessing business potential, a decision was made in April 2002 to liquidate Mako and terminate the license agreement. The Company subsequently licensed the technology to a third party and does not expect to receive significant royalties.

### CURRENT STRATEGY

At present, PublicARD's sole operating activities are conducted through its Infineer subsidiary, which designs smart card platform solutions for educational and corporate sites. The Company's future plans revolve around a potential acquisition strategy focused on businesses in areas outside the high technology sector while continuing to support the expansion of the Infineer business. However, the Company will not be able to implement such plans unless it is successful in obtaining funding, as to which no assurance can be given. Key elements of our strategy include the following:

- **GENERATE CAPITAL.** If the distress termination of the Company's defined benefit pension plan for which the Company has applied is completed (see Note 5 to the Notes to Consolidated Financial Statements), the Company's 2003 funding requirements to the plan could be eliminated, in which case management believes that existing cash and short term investments may be sufficient to meet the Company's operating and capital requirements at the currently anticipated levels through December 31, 2003. However, additional capital will be necessary to fund the current business plan and other obligations and to operate beyond December 2003.

## Edgar Filing: PUBLICARD INC - Form 10-K

While the Company is actively considering various funding alternatives, the Company has not secured or entered into any arrangements to obtain additional funds. There can be no assurance that the Company will eliminate the 2003 funding requirements for the defined benefit pension plan or be able to obtain additional funding on acceptable terms or at all.

- GROW PUBLICARD BUSINESS THROUGH ACQUISITIONS. An important element of the Company's new strategic plan involves the acquisition of businesses in areas outside the technology sectors in which the Company has recently been engaged, so as to diversify its asset base. The Company made a series of successful acquisitions in the 1980's and early 1990's and will endeavor to replicate this success by seeking out businesses meeting a targeted profile. Implementation of this plan will require the Company to obtain funding. However, there can be no assurance that the Company will be able to obtain funding on acceptable terms or at all.
- EXPAND INFINEER MARKET REACH. Management believes that Infineer can expand the market reach of its smart card platform solutions by forming strategic marketing and distribution relationships with a number of key industry players both in the United Kingdom and elsewhere. Infineer has a strong market position in the United Kingdom ("UK") educational sector, and to a lesser extent in the UK corporate market, and intends on leveraging this market position to select markets outside of the U.K.
- EXPAND INFINEER PRODUCT OFFERING. Management believes that Infineer can expand its total product offering, technologies and market position by partnering with companies engaged in complementary businesses or by acquiring or licensing complementary technologies and products. Infineer intends to form relationships, which will provide a "complete" solution to the educational and corporate campus market places.

### PUBLICARD PRODUCTS AND SOLUTIONS

PublicARD designs and develops smart card software and hardware solutions for campus environments. The Company's solutions facilitate card-based payment for a wide variety of services typically found on both corporate and education sites. The Company's products and solutions include the following:

- CHIPNET. The Company provides transaction solutions using a single smart card that facilitate smart card based payments for a wide variety of services typically found on both corporate and educational sites. Implementing a cashless system has many benefits including improved cash flow, enhanced service levels and superior management information. Uniquely adapted to the campus environment and users, ChipNet enables identification, payment at cafeterias, vending machines, photocopiers and printers, and network access to PCs. ChipNet also integrates with third party library management, campus wide access control and time and attendance tracking. The ChipNet solution comprises application software, hardware and smart cards.

On ChipNet sites, card holders load money onto an Infineer multi-application smart card. The card can then be used to pay for cafeteria and vending machine purchases, as well as for copier and networked printer usage. Each time a transaction takes place, all details are recorded, such as the date and time, user and item purchased. These are then processed by a robust back office software package, utilizing a powerful tracking tool that delivers accurate management information on sales and card activity. As the ChipNet solution is based around an open database platform, integration with third party cards, applications and electronic purses can be facilitated quickly and easily. ChipNet is currently installed in over 110 educational and corporate sites, primarily

## Edgar Filing: PUBLICARD INC - Form 10-K

in the United Kingdom.

- CHIPNET QUICKSTART. ChipNet QuickStart is a user-friendly smartcard payment system aimed at libraries and Internet cafes, which will simplify administration and payment for PC log-on, networked printing and photocopying. ChipNet QuickStart has been developed to fill a gap in the market for an entry-level smart card solution providing an administration-free payment system. Although ChipNet QuickStart offers the capacity to run without being networked, it also contains a built-in upgrade path

5

to ChipNet.

- SMARTPRINT CENTRAL. The SmartPrint CENTRAL solution combines a sophisticated print release software package and a card reader to provide a dedicated print release station. The user logs on at any networked PC and, having created or edited their document, sends it across the network to the printer. In order to have the print job printed, the user must physically go to the print release PC, which would typically be located beside the printer, select their print job from the print queue and insert a card for payment. When payment has taken place, the job is printed. SmartPrint CENTRAL is available for the standard card technologies provided by Infineer, namely smart card, revaluable magnetic card and disposable magnetic card.
- EASYCARD. The EasyCard product line delivers a complete and cost effective solution to the problem of vending prints, copies and faxes. Operating with either low cost disposable magnetic cards or rechargeable cards in two formats, slim and ISO standard, EasyCard is a simple to use solution, ideal for schools, colleges, universities, libraries and copy shops. Users carry cards, featuring either a monetary or copy value, and the appropriate amount is deducted each time a service is used. Both analogue and digital copiers can now contribute valuable revenue to institutions by charging for their use. For those customers not paying in advance for services, account cards can be used, recording the use of a range of services against an individual or department. A full range of support products offer card acceptance at vending machines, cafeterias, self-service card centers and encoding stations. EasyCard delivers a range of solutions from "sell and forget" disposable magnetic card operated formats to combination solutions accepting disposable, rechargeable and account cards with full card personalization for access control and time and attendance tracking.
- LICENSED TECHNOLOGY. PubliCARD licenses smart card reader and chip technology to an independent third party. The Company does not expect the revenue stream from the license agreement, which will expire in March 2004, to be significant in the future. PubliCARD developed a line of chips that provide solutions for adding smart card support to a variety of OEM products such as cable set-top boxes, Internet appliances, personal computers and keyboards. These solutions drive the smart card reader in any smart card accepting device, enabling any smart card application and payment transactions to take place. PubliCARD's chips were designed to drive and manage these smart card readers by reading the chip embedded in the card and permitting the stored data to access the proper application. PubliCARD also developed intelligent smart card readers designed for electronic commerce, financial services, access control, security, and a variety of other applications. The reader line included a laptop reader as well as desktop solutions with either a serial or USB interface.



## Edgar Filing: PUBLICARD INC - Form 10-K

### SALES AND MARKETING

PubliCARD sells and distributes its products through a range of distribution channels, including value-added resellers, value-added distributors and other distributors. PubliCARD also sells and distributes its products directly to end-users in the United Kingdom through its direct sales force. PubliCARD has approximately 19 employees directly engaged in the sale, distribution and support of its products in the UK and is represented by 15 independent distributors and resellers.

In support of its sales strategies, PubliCARD also makes use of direct mail campaigns to its customers, advertising in targeted trade media and at trade shows and conferences. PubliCARD intends to continue seeking to form strategic relationships with key industry players to provide it with access to leading edge technology, marketing and sales leverage, and access to key customers and accounts.

### RESEARCH AND DEVELOPMENT

Research and development is a key element to PubliCARD's future success and competitive position. PubliCARD develops an annual technology development plan as an integral part of its business planning process. This plan identifies new areas requiring development in support of identified business opportunities, as well as a program of maintenance and enhancement for PubliCARD's existing solutions.

6

PubliCARD's product development is organized to quickly bring products from concept to product introduction. PubliCARD's future success will depend upon its ability to enhance existing products and to develop and to introduce new products on a timely basis that keep pace with technological developments and emerging industry standards and address the increasingly sophisticated needs of its customers. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Factors That May Affect Future Results -- Our future success depends on our ability to keep pace with technological changes and introduce new products in a timely manner."

### COMPETITION

Competition in the markets in which PubliCARD operates is intense and is characterized by rapidly changing technologies, evolving industry standards, frequent new product introductions and rapid changes in customer requirements. To maintain and improve its competitive position, PubliCARD must continue to develop and introduce, on a timely and cost-effective basis, new products and product features that keep pace with technological developments and emerging industry standards and address the increasingly sophisticated needs of its customers. The principal competitive factors affecting the market for PubliCARD's technology products are the product's technical characteristics and price, customer service and competitor reputation, as well as competitor reputation positioning and resources. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Factors That May Affect Future Results -- The highly competitive markets in which we operate could have a material adverse effect on our business and operating results." PubliCARD will be required to continue to respond promptly and effectively to the challenges of technological changes and its competitors' innovations.

The market for smart card technology solutions is new, intensely competitive and rapidly evolving. PubliCARD expects competition to continue to

## Edgar Filing: PUBLICARD INC - Form 10-K

increase both from existing competitors and new market entrants. PublicARD's primary competition currently comes from or is anticipated to come from companies offering campus environment solutions, including small value electronic cash systems and database management solutions, such as Girovend, MARS, Cunninghams, Uniware, Diebold, and Schlumberger.

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

### INTELLECTUAL PROPERTY

PublicARD's success depends significantly upon its proprietary technology. PublicARD relies on a combination of patent, copyright and trademark laws, trade secrets, confidentiality agreements and contractual provisions to protect its proprietary rights. PublicARD seeks to protect its software, documentation and other written materials under trade secret and copyright laws, which afford only limited protection. PublicARD generally enters into confidentiality and non-disclosure agreements with its employees and with key vendors and suppliers. Despite PublicARD's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of PublicARD's products or to obtain and use information that PublicARD regards as proprietary. Moreover, effective copyright and trade secret protection may be unavailable or limited in certain foreign countries, making the possibility of misappropriation of PublicARD's proprietary technology more likely. The steps taken by PublicARD to protect its proprietary technology might not prevent misappropriation of such technology, and such protections may not preclude competitors from developing products with functionality or features similar to PublicARD's products.

PublicARD currently has various trademarks and trademark applications registered and pending in the

7

United States. PublicARD will continue to evaluate the registration of additional trademarks as it deems appropriate. While PublicARD currently has a number of patents issued and various patent applications pending, it doesn't believe that these patents are of benefit to current operations. There can be no assurance that any new patents will be issued, that PublicARD will develop proprietary products or technologies that are patentable, that any issued patent will provide PublicARD with any competitive advantages or will not be challenged by third parties or that the patents of others will not have a material adverse effect on PublicARD's business and operating results.

In the event that PublicARD's technology or products are determined to infringe upon the rights of others, PublicARD could be required to cease using such technology and stop selling such products, if PublicARD is unable to obtain licenses to utilize such technology. There can be no assurance that PublicARD would be able to obtain such licenses in a timely manner on acceptable terms and conditions, and the failure to do so could have a material adverse effect on PublicARD's financial condition and results of operations. If PublicARD is unable to obtain such licenses, it could encounter significant delays in product

## Edgar Filing: PUBLICARD INC - Form 10-K

market introductions while it attempted to design around the infringed-upon patents or rights, or could find the development, manufacture or sale of products requiring such license to be foreclosed. In addition, patent disputes are common in the smart card and computer industries and there can be no assurance that PublicARD will have the financial resources to enforce or defend a patent infringement or proprietary rights action.

PublicARD expects that software product developers will be increasingly subject to infringement claims as the number of products and competitors in the smart card market grows. Any such claims, with or without merit, could be time-consuming, result in costly litigation and diversion of technical and management personnel, cause product shipment delays or require PublicARD to develop non-infringing technology or enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to PublicARD or at all. In the event of a successful claim of product infringement against PublicARD and failure or inability of PublicARD to develop non-infringing technology or license the infringed or similar technology, PublicARD's business, financial condition and results of operations could be materially adversely affected. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Factors That May Affect Future Results -- Our proprietary technology is difficult to protect and may infringe on the intellectual proprietary rights of third parties."

### EMPLOYEES

As of March 14, 2003, PublicARD had approximately 50 employees, of which 19 are involved in sales, marketing and support, 9 in product development, and 11 in manufacturing. The Company considers its employee relations to be good.

### SEGMENT INFORMATION

As a result of the disposition of certain operations and because the Company operates in one industry, that being the deployment of smart card solutions for educational and corporate sites, the Company reports as a single segment. Sales by geographical areas for the years ended December 31, 2002, 2001 and 2000 are as follows (in thousands):

	2002 ----	2001 ----	2000 ----
United States	\$ 1,029	\$ 1,727	\$ 1,160
Europe	3,445	3,671	4,029
Rest of world	131	254	354
	----- \$ 4,605 =====	----- \$ 5,652 =====	----- \$ 5,543 =====

8

The Company has operations in the United States and United Kingdom. Identifiable assets by country as of December 31, 2002, 2001 and 2000 are as follows (in thousands):

	2002 ----	2001 ----	2000 ----
--	--------------	--------------	--------------

Edgar Filing: PUBLICARD INC - Form 10-K

United States	\$ 4,842	\$12,037	\$25,547
United Kingdom	2,235	2,557	2,866
	-----	-----	-----
	\$ 7,077	\$14,594	\$28,413
	=====	=====	=====

See also the Company's Financial Statements beginning on page F-1.

ITEM 1A. EXECUTIVE OFFICERS OF THE REGISTRANT (SEE ITEM 10 HEREIN)

The following table sets forth information about the executive officers of the Company as of March 15, 2003. The business address of each executive officer is the address of the Company, 620 Fifth Avenue, New York, New York 10020.

Name	Age	Office and Position
Harry I. Freund	63	Director, Chairman of the Board and Chairman
Jay S. Goldsmith	59	Director, Vice Chairman of the Board and Vice Chairman
Antonio L. DeLise	41	Director, President, Chief Executive Officer and Secretary

There is no family relationship between any of the executive officers of the Company. Each officer is elected to serve for a term ending with the next annual meeting of shareholders.

Mr. Freund has been a Director of the Company since April 12, 1985, Chairman of the Board of Directors since December 1985 and Chairman since October 1998. Since 1975, Mr. Freund has been Chairman of Balfour Investors Inc. ("Balfour"), a merchant banking firm that had previously been engaged in a general brokerage business.

Mr. Goldsmith has been a Director of the Company since April 12, 1985, Vice Chairman of the Board of Directors since December 1985 and Vice Chairman since October 1998. Since 1975, Mr. Goldsmith has been President of Balfour.

Mr. DeLise, joined the Company in April 1995 as Vice President, Chief Financial Officer and Secretary. He was appointed to the Board of Directors in July 2001 and was elected to the additional posts of President in February 2002 and Chief Executive Officer in August 2002.

ITEM 2. PROPERTIES

The Company leases the following facilities, which are believed to be adequate for its present needs.

PREMISES	PURPOSE	YEAR OF LEASE EXPIRATION
-----	-----	-----

## Edgar Filing: PUBLICARD INC - Form 10-K

New York, NY  
Bangor, Northern  
Ireland

Executive offices for PublicARD  
Office and manufacturing

2004  
2008

9

The Company and Balfour are parties to an agreement, dated as of October 26, 1994, with respect to a portion of the office space leased by the Company in New York City. The Chairman and Vice Chairman of the Company are the only shareholders of Balfour. The term of the agreement commenced on January 1, 1995 and will expire on June 30, 2004, unless sooner terminated pursuant to law or the terms of the agreement. The agreement provides for Balfour to pay to the Company a portion of the rent paid by the Company under its lease, including base rent, electricity, water, real estate tax escalations and operation and maintenance escalations. Effective March 1, 2002, Balfour's share of rent and other costs was 50% of the total costs incurred. The base rent payable by Balfour under the agreement is approximately \$11,000 per month.

### ITEM 3. LEGAL PROCEEDINGS

On May 28, 2002, a lawsuit was filed against the Company in the Superior Court of the State of California, in the County of Los Angeles by Leonard M. Ross and affiliated entities alleging, among other things, misrepresentation and securities fraud. The lawsuit names the Company and four of its current and former executive officers and directors as the defendants. The plaintiffs seek monetary and punitive damages for alleged actions made by the defendants in order to induce the plaintiff to purchase, hold or refrain from selling PublicARD common stock. The plaintiffs allege that the defendants made a series of material misrepresentations, misleading statements, omissions and concealments, specifically and directly to the plaintiffs concerning the nature, existence and status of contracts with certain purchasers, the nature and existence of investments in the Company by third parties, the nature and existence of business relationships and investments by the Company.

Notice of the commencement of this action has been given to the Company's directors and officers liability insurance carriers. The Company believes it has meritorious defenses to the allegations and intends to defend vigorously. In November 2002, the Company and the individual defendants served with the action filed a demurrer seeking the dismissal of six of the plaintiffs' nine purported causes of action. In January 2003, the court ruled in favor of the demurrer and dismissed the entire complaint. The plaintiffs were granted the right to replead and subsequently filed an amended complaint in February 2003. The Company and individual defendants filed a second demurrer in March 2003. The lawsuit is in the early stages. There has been no discovery and no trial date has been set. Consequently, at this time it is not reasonably possible to estimate the damage, or range of damages, if any, that the Company might incur in connection with this action. However, if the outcome of this lawsuit is unfavorable to the Company, it could have a material adverse effect on the Company's operations, cash flow and financial position. Through December 31, 2002, the Company has incurred approximately \$200,000 in defense costs.

Various other legal proceedings are pending against the Company. The Company considers all such other 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 these claims to the extent not covered by insurance will not, individually or in the aggregate, have a material adverse effect on the consolidated financial position or consolidated results of operations of the Company.

## Edgar Filing: PUBLICARD INC - Form 10-K

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On December 17, 2002, an annual meeting of shareholders of the Company was held at which directors were elected to serve until their successors shall have been elected and shall have qualified. The appointment of Deloitte & Touche LLP as the Company's outside auditors for the year ending December 31, 2002 was also ratified. The voting results were as follows:

Election of directors -----	For ---	Against -----	Abstain -----
Harry I. Freund	15,766,314	--	1,142,252
Jay S. Goldsmith	15,766,014	--	1,142,552
Clifford B. Cohn	15,733,564	--	1,135,002
L.G. Schafran	15,773,864	--	1,134,702
Emil Vogel	15,733,664	--	1,134,902
Antonio L. DeLise	15,733,864	--	1,134,702
 Ratification of auditors	 16,713,264	 184,816	 10,504

10

### PART II

### ITEM 5. MARKET FOR THE REGISTRANT'S COMMON STOCK AND RELATED SECURITY HOLDER MATTERS

- (a) PubliCARD's common stock was listed on the Nasdaq National Market from December 22, 1998 to May 1, 2002. Effective May 2, 2002, the listing of PubliCARD common stock was transferred to the Nasdaq SmallCap Market. The following table sets forth the high and low closing sale prices of PubliCARD's common stock, as reported by the Nasdaq System, for the calendar periods indicated (in dollars):

	2002 ----		2001 ----	
	HIGH	LOW	HIGH	LOW
First Quarter	.27	.09	2.875	1.437
Second Quarter	.52	.11	1.63	.85
Third Quarter	.26	.10	.88	.25
Fourth Quarter	.31	.08	.45	.24

On March 19, 2003, the Company received a Nasdaq Staff Determination letter indicating that the Company failed to comply with the minimum bid price requirement for continued listing on the Nasdaq SmallCap Market and that the Company's common stock is therefore subject to delisting. The board of directors of the Company decided not to appeal the delisting determination. Effective March 28, 2003, the Company's common stock will no longer be traded on the Nasdaq SmallCap Market. The Company expects that on March 28, 2003 its common stock will begin trading on the OTC Bulletin Board. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Factors That May Affect Future Results - Our stock is being delisted from the Nasdaq System."

## Edgar Filing: PUBLICARD INC - Form 10-K

- (b) There were approximately 2,400 registered holders of record of common stock of the Company as of March 17, 2003.
- (c) The Company did not pay dividends on its common stock during the prior five fiscal years and does not anticipate paying dividends in the foreseeable future.

### RECENT SALES OF UNREGISTERED SECURITIES.

In December 2000, the Company completed the private placement of 525,000 shares of common stock and 790 shares of Class A Preferred Stock, Second Series ("Class A Preferred Stock"), a newly designated series of convertible preferred stock, resulting in aggregate proceeds of \$5.0 million to PublicARD. The securities were sold to institutional investors and other accredited investors in the U.S. and Europe pursuant to Regulations D and S under the Securities Act of 1933, as amended (the "Securities Act"). Each share of Class A Preferred Stock is convertible into 2,500 shares of common stock. Therefore, the shares of common stock issued plus the shares of common stock issuable upon conversion of the Class A Preferred Stock aggregate 2.5 million common shares. The proceeds from the private placement were used to acquire a 3.5% ownership interest in TecSec. The Company registered the shares of common stock issued and the shares of common stock underlying the Class A Preferred Stock for resale under the Securities Act through a registration statement on Form S-3, which became effective on January 22, 2001.

In connection with the December 2000 private placement, the Company issued 100 rights equally to the participants in the private placement pursuant to Regulations D and S under the Securities Act. These rights entitle the participating holders of common stock and Class A Preferred Stock to receive an aggregate of ten percent of any increase in value of the TecSec investment realized by the Company. See Note 2 to the Company's Consolidated Financial Statements for details regarding the Company's investment in TecSec.

11

On July 17, 2000 and October 16, 2000, the Company issued 60,000 and 55,000 shares of common stock, respectively, to the Publicker Industries Inc. Retirement Income Plan pursuant to Regulations D and S under the Securities Act in respect of a \$365,000 required contribution to that Plan. The Company registered the shares issued to such Plan for resale under the Securities Act through a registration statement on Form S-3, which became effective on January 22, 2001.

On February 29, 2000, the Company issued 66,333 shares of common stock for the remaining 35% interest in Greenwald Intellicard not already owned by the Company. The Company registered the shares issued for resale under the Securities Act through a registration statement on Form S-3, which became effective on April 12, 2000.

On January 4, 2000, the Company issued 32,500 shares of common stock to a former employee as part of the separation agreement dated December 3, 1999. The Company registered the shares issued for resale under the Securities Act through a registration statement on Form S-3, which became effective on April 12, 2000.

12

## Edgar Filing: PUBLICARD INC - Form 10-K

### ITEM 6. SELECTED FINANCIAL DATA

The selected financial data of the Company presented below for the five year period ended December 31, 2002 have been derived from the consolidated financial statements of the Company. The information set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Company's Consolidated Financial Statements and the Notes thereto included elsewhere in this Form 10-K.

	Year Ended December 31				
	2002	2001	2000	1999	1998
	(in thousands, except per share amounts)				
<b>STATEMENT OF OPERATIONS DATA:</b>					
Net sales	\$ 4,605	\$ 5,652	\$ 5,543	\$ 1,930	\$ 3
Cost of sales	2,455	2,875	2,913	978	7
Inventory adjustment	--	1,661	--	--	--
	2,150	1,116	2,630	952	(4)
<b>Operating expenses:</b>					
General and administrative	3,235	4,625	6,664	5,713	3,694
Sales and marketing	1,877	3,413	7,562	2,862	21
Product development	605	2,442	4,364	1,318	53
In-process research and development	--	--	--	--	2,800
Stock compensation expense	--	86	1,116	2,759	145
Amortization of goodwill and intangibles	576	1,824	2,638	1,749	128
Impairment of goodwill and intangibles	1,365	--	--	--	--
Repositioning and other special charges	--	5,656	--	1,895	--
	7,658	18,046	22,344	16,296	6,841
Loss from operations	(5,508)	(16,930)	(19,714)	(15,344)	(6,845)
<b>Other income (expenses):</b>					
Interest income	71	476	936	561	528
Interest expense	(39)	(65)	(100)	(158)	(191)
Cost of retirement benefits - non-operating	(795)	(788)	(812)	(1,028)	(846)
Write-down of minority investment	(2,068)	--	--	--	--
Other (expense) income	80	136	15	(751)	(1,023)
	(2,751)	(241)	39	(1,376)	(1,532)
Loss from continuing operations	(8,259)	(17,171)	(19,675)	(16,720)	(8,377)
<b>Discontinued operations:</b>					
Income (loss) from discontinued operations	--	--	--	(13,999)	2,302
Gain (loss) on disposition of					



Edgar Filing: PUBLICARD INC - Form 10-K

discontinued operations	1,066	2,350	4,275	(5,000)	--
	-----	-----	-----	-----	-----
Net loss	\$ (7,193)	\$ (14,821)	\$ (15,400)	\$ (35,719)	\$ (6,075)
	=====	=====	=====	=====	=====
Basic and diluted earnings (loss)					
per common share:					
Continuing operations	\$ (.34)	\$ (.71)	\$ (.84)	\$ .88	\$ (.61)
Discontinued operations	.04	.10	.18	(1.00)	.17
	-----	-----	-----	-----	-----
	(.30)	\$ (.61)	\$ (.66)	\$ (1.88)	\$ (.44)
	=====	=====	=====	=====	=====

13

	As of December 31				
	-----	-----	-----	-----	-----
	2002	2001	2000	1999	1998
	----	----	----	----	----
	(in thousands)				
BALANCE SHEET DATA:					
Working capital (deficiency)	\$ (548)	\$ 2,631	\$13,168	\$23,889	\$23,420
Total assets	7,939	17,397	37,179	45,488	36,875
Other non-current liabilities	4,990	5,328	6,010	6,674	7,689
Shareholders' equity	(1,002)	7,484	23,578	30,399	21,917

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangibles". In accordance with the guidelines of this statement, goodwill and definite lived intangible assets are no longer amortized but will be assessed for impairment on at least an annual basis.

No dividends on common shares have been declared or paid during the last five years.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

PubliCARD 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 (the "Board"), 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 adopted a plan of disposition pursuant to which the Company divested its non-core operations. See Note 9 to the Consolidated Financial Statements for a discussion on the disposition plan.

In July 2001, after evaluating the timing of potential future revenues, PubliCARD's Board decided to shift the Company's strategic focus. While the

## Edgar Filing: PUBLICARD INC - Form 10-K

Board remained confident in the long-term prospects of the smart card business, the timing of public sector and corporate initiatives in wide-scale, broadband environments utilizing the Company's smart card reader and chip products had become more uncertain. Given the lengthened time horizon, the Board did not believe it would be prudent to continue to invest the Company's current resources in the ongoing development and marketing of these technologies. Accordingly, the Board determined that shareholders' interests will be best served by pursuing strategic alliances with one or more companies that have the resources to capitalize more fully on the Company's smart card reader and chip-related technologies. In connection with this shift in the Company's strategic focus, workforce reductions and other measures were implemented to achieve cost savings. See Note 10 to the Consolidated Financial Statements for a discussion on the repositioning charge associated with this action.

At present, PublicARD's sole operating activities are conducted through its Infineer Ltd. ("Infineer") subsidiary, which designs smart card platform solutions for educational and corporate sites. The Company's future plans revolve around a potential acquisition strategy that would focus on businesses in areas outside the high technology sector while continuing to support the expansion of the Infineer business. However, the Company will not be able to implement such plans unless it is successful in obtaining additional funding, as to which no assurance can be given.

PublicARD's financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the Consolidated Financial Statements, the Company has incurred operating losses, has a working capital deficiency and requires additional capital to meet its obligations and

14

accomplish the Company's business plan, which raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the Company's failure to obtain funding or inability to continue as a going concern.

### RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2002 COMPARED TO YEAR ENDED DECEMBER 31, 2001

**SALES.** Revenues are generated from product sales, technology and software license fees, installation and maintenance contracts. Consolidated sales decreased to \$4.6 million in 2002 compared to \$5.7 for 2001. The 2001 figure included \$1.0 million of revenues associated with the smart card reader and chip business, which the Company exited in July 2001. Sales related to smart card solutions for educational and corporate sites were comparable between years.

**GROSS MARGIN.** Cost of sales consists primarily of material, personnel costs and overhead. Cost of sales in 2001 included an adjustment of \$1.7 million for the write-off of inventories associated with the July 2001 repositioning action. Excluding the inventory adjustment, gross margin as a percentage of sales decreased to 47% in 2002 from 49% in 2001.

**SALES AND MARKETING EXPENSES.** Sales and marketing expenses consist primarily of personnel and travel costs, public relations, trade shows and marketing materials. Sales and marketing expenses were \$1.9 million in 2002 compared to \$3.4 million in 2001. The decrease in expense is attributed to the July 2001 repositioning action.

## Edgar Filing: PUBLICARD INC - Form 10-K

PRODUCT DEVELOPMENT EXPENSES. Product development expenses consist primarily of personnel and travel costs, independent consultants and contract engineering services. Product development expenses include expenses associated with the development of new products and enhancements to existing products. Product development expenses amounted to \$605,000 in 2002 compared to \$2.4 million in 2001. The decrease in expense is attributed to the July 2001 repositioning action.

GENERAL AND ADMINISTRATIVE EXPENSES. 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. General and administrative expenses for the year ended December 31, 2002 decreased to \$3.2 million from \$4.6 million for 2001. The decrease in expense is mainly due to corporate cost containment initiatives.

STOCK COMPENSATION EXPENSE. Stock-based compensation recorded in 2001 principally relates to the issuance of stock awards and a below market stock option grant to an executive hired in late 1999.

AMORTIZATION OF GOODWILL AND INTANGIBLES. In accordance Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"), no amortization expense for goodwill will be recorded in current and future periods. Goodwill and other intangibles will be subject to an annual review for impairment or earlier if circumstances or events indicate that impairment has occurred. This may result in future write-downs or the write-off of such assets. Amortization expense in 2002 relates to the continuing amortization of definite lived intangibles. As such, amortization expense decreased from \$1.8 million in 2001 to \$576,000 in 2002.

IMPAIRMENT OF GOODWILL AND INTANGIBLES. The Company performed an initial review for impairment of goodwill as of January 1, 2002 and determined that no impairment existed at that date. The Company determined the fair value of its sole reporting unit primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for several entities with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor.

The Company performed its annual impairment test in the fourth quarter of 2002 and determined that

goodwill had been impaired. The Company determined the fair value primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for an entity with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor. Based on comparing the values derived from the two techniques to the carrying value of the reporting unit, the Company recorded a goodwill impairment loss of \$364,000 in the fourth quarter of 2002. The Company attributes the impairment loss to the value of the comparable entity that was sold in late 2002, the significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to the continued overall decline in technology spending and a shortage of capital available to invest in the

## Edgar Filing: PUBLICARD INC - Form 10-K

reporting unit. On an ongoing basis, the Company expects to perform its annual impairment test during the fourth quarter absent any interim impairment indicators.

In the fourth quarter of 2002, the Company determined that its intangible assets had been impaired and recorded an impairment loss of \$1.0 million. The Company attributes the impairment loss to the significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to a continued overall decline in technology spending and a shortage of capital available to invest in the reporting unit.

OTHER INCOME AND EXPENSE. Interest income decreased to \$71,000 from \$476,000 in the prior year principally due to lower investment balances. Cost of pensions, which represents amounts related to discontinued product lines and related plant closings in prior years, principally relates to pension expense associated with the Company's frozen defined benefit pension plan. In addition, in 2002 other expenses included a \$2.1 million charge for an impairment of the Company's minority investment in TecSec. The Company attributes the impairment to a general decline in valuations of technology entities, the difficulties in raising capital and TecSec's recurring operating losses.

YEAR ENDED DECEMBER 31, 2001 COMPARED TO YEAR ENDED DECEMBER 31, 2000

SALES. Consolidated sales increased to \$5.7 million in 2001 compared to \$5.5 million for 2000. The increase is primarily attributed to sales of smart card readers for security applications.

GROSS MARGIN. Gross margin as a percentage of sales was 20% for 2001 (49% excluding the inventory adjustment discussed below) compared to 47% for 2000. Excluding the inventory adjustment, the gross margin percentage increase is principally due to improved margins on smart card reader sales.

SALES AND MARKETING EXPENSES. Sales and marketing expenses were \$3.4 million in 2001 compared to \$7.6 million in 2000. The decrease is attributed to the July 2001 repositioning action, additional headcount reductions throughout 2000 and 2001 and lower consulting expenses for market research and corporate branding.

PRODUCT DEVELOPMENT EXPENSES. Product development expenses amounted to \$2.4 million in 2001 compared to \$4.4 million in 2000. The decrease in expense is attributed to the July 2001 repositioning action, headcount reductions throughout 2000 and 2001 and lower contract engineering services costs.

GENERAL AND ADMINISTRATIVE EXPENSES. General and administrative expenses for the year ended December 31, 2001 decreased to \$4.6 million from \$6.7 million for 2000. The decrease in expense is attributed to the July 2001 repositioning action, headcount reductions and lower corporate expenditures, which consisted primarily of legal, consulting and professional fees.

STOCK COMPENSATION EXPENSE. Stock-based compensation recorded in 2001 and 2000 principally relates to the issuance of stock awards and below market stock option grants to two executives hired in 2000 and 1999.

AMORTIZATION OF GOODWILL AND INTANGIBLES. Goodwill and intangibles are amortized on a straight-line basis over five years. Amortization decreased to \$1.8 million in 2001 from \$2.6 million in 2000 due to the write-off of the remaining goodwill and intangibles associated with the smart card reader and chip business in the second quarter of 2001.

REPOSITIONING CHARGE. As discussed above in July 2001, after evaluating the timing of potential future revenues, PublicARD's Board decided to shift the Company's strategic focus. The Company recorded a

charge aggregating \$7.3 million in the second and third quarters of 2001 associated with the departure from the smart card reader and chip business. The charge consisted of write-offs of goodwill and intangibles of \$4.1 million and fixed assets of \$554,000, an inventory realizability adjustment of \$1.7 million (included in cost of sales) as a result of the business closure, and severance and other costs of \$1.0 million principally related to the termination of 36 employees. The repositioning activities were substantially completed by December 31, 2001.

OTHER INCOME AND EXPENSE. Interest income decreased to \$476,000 from \$936,000 in the prior year due to lower interest rates and investment balances. Interest expense principally relates to interest on the remaining environmental obligation and decreased to \$65,000 in 2001 from \$100,000 in 2000. Cost of pensions principally relates to pension expense associated with the Company's frozen defined benefit pension plan.

#### LIQUIDITY

The Company has financed its operations over the last three years primarily through the sale of capital stock and the sale of non-core businesses. During the year ended December 31, 2002, cash, including short-term investments, decreased by \$3.2 million to \$1.3 million as of December 31, 2002.

Operating activities utilized cash of \$5.1 million in 2002 and principally consisted of the net loss of \$7.2 million plus a non-cash gain on discontinued operations of \$1.1 million offset by \$2.1 million minority investment impairment, a decrease in assets and liabilities of \$1.0 million, an impairment of goodwill and intangibles of \$1.4 million and depreciation and amortization of \$781,000.

Investing activities provided cash of \$1.9 million in 2002 and consisted principally of the release of escrowed funds in connection with previously discontinued operations offset in part by capital expenditures.

The Company has experienced negative cash flow from operating activities in the past and expects to experience negative cash flow in 2003 and beyond. In addition to funding operating and capital requirements and corporate overhead, future uses of cash include the following:

- The Company sponsors a defined benefit pension plan, which was frozen in 1993. As of December 31, 2002, the actuarial present value of accrued liabilities exceeded the plan assets by approximately \$6.1 million. The annual required contribution to the plan is expected to be approximately \$1.5 million in 2003. Since the plan is significantly underfunded, absent some action by the Company, the annual contribution requirements beyond 2003 would continue to be significant. In view of its financial condition, in January 2003, the Company filed a notice with the Pension Benefit Guaranty Corporation ("PBGC") seeking a "distress termination" of the Plan. If the PBGC determines that the Company meets one of the tests for such a termination, the Plan will terminate and the PBGC will become responsible for meeting future retirement obligations to participants (within certain limitations). The Company would be liable to the PBGC for the amount of the unfunded guaranteed benefit obligation. The Company believes that on a termination basis, the Plan's liabilities could exceed the value of its assets by in excess of \$7.0 million. In addition, the Company did not make the required

## Edgar Filing: PUBLICARD INC - Form 10-K

quarterly contribution of approximately \$253,000 that was due on January 15, 2003. The Company has initiated discussions with the PBGC concerning the termination of the Plan and its repayment obligation to the PBGC if the Plan is terminated (including the timing of its repayment obligation). It is not possible to predict the outcome of such discussions.

- The Company and certain current and former officers are defendants in a lawsuit alleging, among other things, misrepresentation and securities fraud. The Company believes that it has meritorious defenses to the allegations and intends to defend itself vigorously. The cost of defending against this action could be significant, and if the Company is not successful in defending itself, the Company may be required to pay the plaintiff's damages, which could have a material adverse effect on the Company's business and operations.

17

- The Company leases certain office space, vehicles and office equipment under operating leases that expire over the next six years. Minimum payments for operating leases having initial or remaining non-cancelable terms in excess of one year are \$422,000 in 2003, \$210,000 in 2004, \$64,000 in 2005, \$55,000 in 2006, \$55,000 in 2007 and \$40,000 thereafter.

The Company will need to raise additional capital that may not be available to it. If the distress termination of the Company's defined benefit pension plan for which the Company has applied is completed (see Note 5 to the Notes to Consolidated Financial Statements), the Company's 2003 funding requirements to the plan could be eliminated, in which case management believes that existing cash and short term investments may be sufficient to meet the Company's operating and capital requirements at the currently anticipated levels through December 31, 2003. However, additional capital will be necessary in order to operate beyond December 2003 and to fund the current business plan and other obligations. While the Company is actively considering various funding alternatives, it has not secured or entered into any arrangements to obtain additional capital. There can be no assurance that the Company will eliminate the 2003 funding requirements for the defined benefit pension plan or be able to obtain additional funding on acceptable terms or at all. If the Company cannot raise additional capital to continue its present level of operations it may not be able to meet its obligations, take advantage of future acquisition opportunities or further develop or enhance its product offering, any of which could have a material adverse effect on its business and results of operations.

The Company currently has no capacity for commercial debt financing. Should such capacity become available it may be adversely affected in the future by factors such as higher interest rates, inability to borrow without collateral, and continued operating losses. Borrowings may also involve covenants limiting or restricting its operations or future opportunities.

As a result of a failure to meet certain continuing listing requirements of the Nasdaq National Market ("National Market"), the Company transferred the listing of its common stock to the Nasdaq SmallCap Market ("SmallCap Market") effective May 2, 2002. On March 19, 2003, the Company received a Nasdaq Staff Determination letter indicating that the Company failed to comply with the minimum bid price requirement for continued listing on the SmallCap Market and that the Company's common stock is therefore subject to delisting. The board of directors of the Company decided not to appeal the delisting determination. Effective March 28, 2003, the Company's common stock will no longer be traded on

## Edgar Filing: PUBLICARD INC - Form 10-K

the Nasdaq SmallCap Market. The Company expects that on March 28, 2003 its common stock will begin trading on the OTC Bulletin Board. As a result of the delisting, the liquidity of the common stock may be adversely affected. This could impair the Company's ability to raise capital in the future. If additional capital is raised through the issuance of equity securities, the Company's stockholders' percentage ownership of the common stock will be reduced and stockholders may experience dilution in net book value per share, or the new equity securities may have rights, preferences or privileges senior to those of its common stockholders.

If the Company's liquidity does not improve, it may be unable to continue as a going concern and could seek bankruptcy protection. Such an event may result in the Company's common and preferred stock being negatively affected or becoming worthless. The auditors' report on the Company's Consolidated Financial Statements for the year ended December 31, 2002 contains an emphasis paragraph concerning substantial doubt about the Company's ability to continue as a going concern.

### CRITICAL ACCOUNTING POLICIES

The Company's significant accounting policies are more fully described in the Notes to the Company's Consolidated Financial Statements. Certain accounting policies require the application of significant judgment by management in selecting the appropriate assumptions for calculating financial estimates. By their nature, these judgments are subject to an inherent degree of uncertainty. The Company considers certain accounting policies related to revenue recognition, estimates of reserves for receivables and inventories, valuation of investments and goodwill and intangibles and pension accounting to be critical policies due to the estimation processes involved.

18

**REVENUE RECOGNITION AND ACCOUNTS RECEIVABLE.** Revenue from product sales and technology and software license fees is recorded upon shipment if a signed contract exists, the fee is fixed and determinable, the collection of the resulting receivable is probable and the Company has no obligation to install the product or solution. If the Company is responsible for installation, revenue from product sales and license fees is recognized upon client acceptance or "go live" date. Revenue from maintenance and support fees is recognized ratably over the contract period. Provisions are recorded for estimated warranty repairs and returns at the time the products are shipped. Should changes in conditions cause management to determine that revenue recognition criteria are not met for certain future transactions, revenue recognized for any reporting period could be adversely affected.

The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's credit worthiness. The Company continually monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that it has identified. While such credit losses have historically been within management's expectations and the provisions established, there is no assurance that the Company will continue to experience the same credit loss rates as in the past.

**INVENTORIES.** Inventories are stated at lower of cost (first-in, first-out method) or market. The Company periodically evaluates the need to record adjustments for impairment of inventory. 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 management's estimates related to the Company's production schedules, customer demand,

## Edgar Filing: PUBLICARD INC - Form 10-K

possible alternative uses and the ultimate realization of potentially excess inventory. During 2001, the decision to exit the smart card reader and chip business resulted in a significant inventory realizability adjustment. While management deems this adjustment to be non-recurring, a decrease in future demand for current products could result in an increase in the amount of excess inventories on hand.

**VALUATION OF INVESTMENTS.** The Company periodically assesses the carrying value of its minority-owned investments for impairment. This assessment is based upon a review of operations and indications of continued viability, such as subsequent rounds of financing. As discussed in Note 2 to the Consolidated Financial Statements, during 2002 the Company made a determination that its minority-owned investments in TecSec and Mako were impaired. While management believes that the adjusted carrying value of its investment in TecSec is fairly stated, future circumstances could affect the valuation.

**IMPAIRMENT OF GOODWILL AND INTANGIBLES.** Effective January 1, 2002, the Company adopted SFAS No. 142. In accordance with the guidelines of this statement, goodwill and indefinite lived intangible assets are no longer amortized but will be assessed for impairment on at least an annual basis. SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives and reviewed for impairment. The Company performed an initial review for impairment of goodwill as of January 1, 2002 and determined that no impairment existed at that date. The Company determined the fair value of its sole reporting unit primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for several entities with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor.

The Company performed its annual goodwill impairment test in the fourth quarter of 2002 and determined that goodwill had been impaired. The Company determined the fair value primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for an entity with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor. Based on comparing the values derived from the two techniques to the carrying value of the reporting unit, the Company recorded a goodwill impairment loss of \$364,000 in the fourth quarter of 2002. The Company attributes the impairment loss to the value of a comparable entity that was sold in a transaction in late 2002, the

19

significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to a continued overall decline in technology spending and a shortage of capital available to invest in the reporting unit. On an ongoing basis, the Company expects to perform its annual impairment test during the fourth quarter absent any interim impairment indicators.

Long-lived assets and certain identifiable intangible assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition.



## Edgar Filing: PUBLICARD INC - Form 10-K

Measurement of any impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the net realizable of the asset. In the fourth quarter of 2002, the Company determined that its intangible assets had been impaired and recorded an impairment loss of \$1.0 million. The Company attributes the impairment loss to the significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to a continued overall decline in technology spending and a shortage of capital available to invest in the reporting unit.

PENSION OBLIGATIONS. The determination of obligations and expense for pension benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. These assumptions include, among others, the discount rate and the expected rate of return on plan assets. Actual results that differ from assumptions are accumulated and amortized over future periods and therefore, generally affect the recognized expense and recorded obligation in such future periods. While management believes that the assumptions are appropriate, differences in actual experience or significant changes in assumptions may materially affect the pension obligation and future expense.

### RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued SFAS No. 141, "Business Combinations". SFAS No. 141 addresses financial accounting and reporting for business combinations. This new statement requires that all business combinations be accounted for using one method (the purchase method), intangible assets be recognized apart from goodwill if they meet certain criteria and disclosure of the primary reasons for a business combination and the allocation of the purchase price paid to the assets acquired and liabilities assumed by major balance sheet caption. The provisions of this statement apply to all business combinations initiated after June 30, 2001.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets". SFAS No. 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets. Under this new statement, goodwill and intangible assets that have indefinite useful lives will not be amortized, but rather will be tested at least annually for impairment, or earlier if circumstances or events indicate that impairment may have occurred, based on the specific guidance of this statement. This may result in future write-downs or the write-off of such assets. In addition, this statement requires disclosure of information about goodwill and other intangible assets in the years subsequent to their acquisition that was not previously required. The provisions of this statement are required to be applied starting with fiscal years beginning after December 15, 2001. However, goodwill and intangible assets acquired after June 30, 2001 were subject immediately to the non-amortization and amortization provisions of this statement. The Company adopted this statement on January 1, 2002. The Company completed the initial impairment test in the first quarter of 2002, which did not result in an impairment of goodwill. The provisions of SFAS No. 142 are effective for periods after adoption and retroactive application is not permitted. Therefore, the historical results of periods prior to 2002 in the Company's Consolidated Statements of Operations do not reflect the effect of SFAS No. 142 and, accordingly, 2001 and 2000 included goodwill amortization expense of \$1.1 million and \$1.7 million, respectively. Excluding goodwill amortization, the pro forma net loss for 2001 and 2000 was \$13.7 million and \$13.7 million or \$.57 and \$.59 per share, respectively.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supercedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of", and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations - Reporting the Effects of

Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions", for the disposal of a segment of a business. This statement also amends ARB No. 51, "Consolidated Financial Statements", to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary. The provisions of this statement are required to be applied starting with fiscal years beginning after December 15, 2001. The Company adopted SFAS No. 144 in the first quarter of fiscal 2002, which did not have an effect on the Company's results of operations or financial position.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". SFAS No. 146 will supersede Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)". SFAS No. 146 requires that costs associated with an exit or disposal plan be recognized when incurred rather than at the date of a commitment to an exit or disposal plan. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The Company does not believe that the adoption of SFAS No. 146 will have a material effect on its Consolidated Financial Statements.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure". SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation", to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock based employee compensation and the effect of the method used on reported results. The provisions of SFAS No. 148 are effective for financial statements for fiscal years and interim periods ending after December 15, 2002. The disclosure provisions of SFAS No. 148 have been adopted by the Company. See Note 1 to the Consolidated Financial Statements. SFAS No. 148 did not require the Company to change to the fair value based method of accounting for stock-based compensation.

#### FACTORS THAT MAY AFFECT FUTURE RESULTS

WE HAVE A HISTORY OF OPERATING LOSSES AND NEGATIVE CASH FLOW, WE HAVE ONGOING FUNDING OBLIGATIONS AND WE NEED TO RAISE ADDITIONAL CAPITAL THAT MAY NOT BE AVAILABLE TO US, ALL OF WHICH COULD LEAD US TO SEEK BANKRUPTCY PROTECTION. 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 2000, 2001 and 2002 of approximately \$19.7 million, \$17.2 million and \$8.3 million, respectively. In addition, we experienced negative cash flow from continuing operating activities of \$18.7 million, \$12.2 million and \$5.1 million in 2000, 2001 and 2002, respectively, and have a working capital deficiency of \$548,000 as of December 31, 2002.

We sponsor a defined benefit pension plan (the "Plan"), which was frozen in 1993. As of December 31, 2002, the present value of the accrued benefit liabilities of our pension plan exceeded the Plan's assets by approximately \$6.1 million. The annual required contribution to the Plan is expected to be \$1.5 million for 2003 and if the Plan is continued, we will be obligated to make continued contributions in accordance with the Employee Retirement Income Security Act of 1974. Since the Plan is significantly underfunded, absent some action by us, we expect that the annual contribution requirements beyond 2003

## Edgar Filing: PUBLICARD INC - Form 10-K

will continue to be significant. Future contribution levels depend in large measure on the mortality rate of plan participants, discount rate and the expected return on the plan assets. In April 2002, we failed to make the required quarterly contribution to the Plan due April 15, 2002, in the amount of \$253,000. We paid this required contribution on June 11, 2002. Quarterly contributions of \$253,000 each were made on a timely basis in July 2002 and October 2002. In view of our financial condition, in January 2003, we filed a notice with the Pension Benefit Guaranty Corporation ("PBGC") seeking a "distress termination" of the Plan and did not make the quarterly contribution of approximately \$253,000 due on January 15, 2003. If the PBGC determines that we meet one of the tests for such termination, the Plan will terminate and the PBGC will become responsible for meeting future retirement obligations to participants (within certain limitations). We would be liable to the PBGC for the amount of the unfunded benefit obligation. We believe that, on a

21

termination basis, the Plan's liabilities could exceed the value of its assets by in excess of \$7.0 million. We have initiated discussions with the PBGC concerning the termination of the Plan and our repayment obligation to the PBGC if the Plan is terminated (including the timing of our repayment obligation). It is not possible to predict the outcome of such discussions.

We and certain current and former officers are defendants in a lawsuit alleging, among other things, misrepresentation and securities fraud. We believe that we have meritorious defenses to the allegations and intend to defend ourselves vigorously. The cost of defending against this action could be significant, and if the Company is not successful in defending itself, the Company may be required to pay the plaintiff's damages, which could have a material adverse effect on the Company's business and operations. See "We are unable to predict the extent to which the resolution of lawsuits pending against us could adversely affect our business". In addition, we have future non-cancelable operating lease obligations for office space, vehicles and office equipment aggregating \$846,000.

We will need to raise additional capital that may not be available to us. If the distress termination of our defined benefit pension plan for which we have applied is completed, our 2003 funding requirements discussed above could be eliminated, in which case, we believe that existing cash and short term investments may be sufficient to meet our operating and capital requirements at the currently anticipated level through December 31, 2003. However, additional capital will be necessary in order to operate beyond December 2003 and to fund the current business plan and other obligations. While we are actively considering various funding alternatives, no arrangement to obtain additional funding has been secured or entered into. There can be no assurance that we will eliminate the 2003 funding requirements for the defined benefit pension plan or be able to obtain additional funding, on acceptable terms or at all. If we cannot raise additional capital to continue at our present level of operations we may not be able to meet our obligations, take advantage of future acquisition opportunities or further develop or enhance our product offering, any of which could have a material adverse effect on our business and results of operations and could lead us to seek bankruptcy protection. The auditors' reports on the Company's Consolidated Financial Statements for the years ended December 31, 2001 and 2002 contained an emphasis paragraph concerning substantial doubt about the Company's ability to continue as a going concern.

We currently have no capacity for commercial debt financing. Should such capacity become available to us, we may be adversely affected in the future by factors such as higher interest rates, inability to borrow without collateral, and continued operating losses. Borrowings may also involve covenants limiting

## Edgar Filing: PUBLICARD INC - Form 10-K

or restricting our operations or future opportunities.

OUR STOCK IS BEING DELISTED FROM THE NASDAQ SYSTEM. On February 14, 2002, we received a notice from The Nasdaq Stock Market ("Nasdaq") that our common stock had failed to maintain a minimum closing bid price of \$1.00 over the last 30 consecutive trading days as required by National Market rules. We received a second notice on February 27, 2002, that our common stock also failed to maintain a market value of public float of \$5 million.

In accordance with the Nasdaq rules, we were required to regain compliance with the National Market minimum bid price requirement and with the market value of public float requirement by May 2002. Since our common stock continued to trade significantly below \$1.00, in April 2002, we filed an application to transfer the listing of our common stock to the SmallCap Market. The application was approved and our common stock listing was transferred to the SmallCap Market effective May 2, 2002. The SmallCap Market also has a minimum bid price requirement of \$1.00. We qualified for an extended grace period to comply with the SmallCap Market's \$1.00 minimum bid price requirement, which extended the delisting determination by Nasdaq until February 10, 2003.

On March 19, 2003, we received a Nasdaq Staff Determination letter indicating that we failed to comply with the minimum bid price requirement for continued listing on the SmallCap Market and that our common stock is therefore subject to delisting. Our board of directors decided not to appeal the delisting determination. Effective March 28, 2003, our common stock will no longer be traded on the SmallCap Market. We expect that on March 28, 2003, our common stock will begin trading on the OTC Bulletin Board.

22

As a result of the delisting, the liquidity of our common stock may be materially adversely affected. Also, there is no certainty that market makers will choose to make a market for our common stock on the OTC Bulletin Board. This could impair our ability to raise capital in the future. There can be no assurance that we will be able to obtain additional funding, on acceptable terms or at all. If we cannot raise additional capital to continue at our present level of operations we may not be able to meet our obligations, take advantage of future acquisition opportunities or further develop or enhance our product offering, any of which could have a material adverse effect on our business and results of operations and could lead us to seek bankruptcy protection.

WE ARE UNABLE TO PREDICT THE EXTENT TO WHICH THE RESOLUTION OF LAWSUITS PENDING AGAINST US COULD ADVERSELY AFFECT OUR BUSINESS. On May 28, 2002, a lawsuit was filed against us in the Superior Court of the State of California, in the County of Los Angeles by Leonard M. Ross and affiliated entities alleging, among other things misrepresentation and securities fraud. The lawsuit names four of our current and former executive officers and directors and us as the defendants. The plaintiffs seek monetary and punitive damages for alleged actions made by the defendants in order to induce the plaintiff to purchase, hold or refrain from selling PublicARD common stock. The plaintiffs allege that the defendants made a series of material misrepresentations, misleading statements, omissions and concealments, specifically and directly to the plaintiffs concerning the nature, existence and status of contracts with certain purchasers, the nature and existence of investments in us by third parties, the nature and existence of business relationships and investments by us.

Notice of the commencement of this action has been given to our directors and officers liability insurance carriers. We believe we have meritorious defenses to the allegations and we intend to defend ourselves vigorously. In November 2002, we and the individual defendants served with the action filed a

## Edgar Filing: PUBLICARD INC - Form 10-K

demurrer seeking the dismissal of six of the plaintiffs' nine purported causes of action. In January 2003, the court ruled in favor of the demurrer and dismissed the entire complaint. The plaintiff has the right to replead and subsequently filed an amended complaint in February 2003. We and individual defendants filed a second demurrer in March 2003. The lawsuit is in the early stages. There has been no discovery and no trial date has been set. Consequently, at this time it is not reasonably possible to estimate the damage, or range of damages, if any, that we might incur in connection with this action. However, if the outcome of this lawsuit is unfavorable to us, it could have a material adverse effect on our operations, cash flow and financial position. Through December 31, 2002, the Company has incurred approximately \$200,000 in defense costs.

WE FACE RISKS ASSOCIATED WITH ACQUISITIONS. An important element of our new strategic plan involves the acquisition of businesses in areas outside the technology sectors in which we have recently been engaged, so as to diversify our asset base. However, we will only be able to engage in future acquisitions if we are successful in obtaining additional funding, as to which no assurance can be given. Acquisitions would require us to invest financial resources and may have a dilutive effect on our earnings or book value per share of common stock. We cannot assure you that we will consummate any acquisitions in the future, that any financing required for such acquisitions will be available on acceptable terms or at all, or that any past or future acquisitions will not materially adversely affect our results of operations and financial condition.

Our acquisition strategy generally presents a number of significant risks and uncertainties, including the risks that:

- we will not be able to retain the employees or business relationships of the acquired company;
- we will fail to realize any synergies or other cost reduction objectives expected from the acquisition;
- we will not be able to integrate the operations, products, personnel and facilities of acquired companies;
- management's attention will be diverted to pursuing acquisition opportunities and integrating acquired products, technologies or companies and will be distracted from performing its regular responsibilities;

23

- we will incur or assume liabilities, including liabilities that are unknown or not fully known to us at the time of the acquisition; and
- we will enter markets in which we have no direct prior experience.

We cannot assure you that any of the foregoing will not materialize, which could have an adverse effect on our results of operations and financial condition.

OUR TECSEC INVESTMENT MAY BE IMPAIRED OR SUBJECT TO A SIGNIFICANT WRITE-DOWN IN THE FUTURE. As of December 31, 2002, after recording an impairment charge of \$2.1 million in the third quarter of 2002, the carrying value of our investment in TecSec, a privately held company, was \$3.0 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 executing its business plan or in obtaining sufficient capital on acceptable terms or at all, our investment in TecSec could be further impaired and subject to an additional significant write-down.

## Edgar Filing: PUBLICARD INC - Form 10-K

THE MARKET'S ACCEPTANCE OF OUR PRODUCTS IS UNCERTAIN. Demand for, and market acceptance of, our software solutions and products 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 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 future revenues and earnings depend in large part on the success of these products, and if the benefits are not perceived sufficient or if alternative technologies are more widely accepted, 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 year ended December 31, 2002, one customer represented approximately 10% of our sales. Amounts due from a second customer represented approximately 12% of the accounts receivable balance as of December 31, 2002.

We generally do not enter into long-term supply commitments with our customers. Instead, we bid on a project basis. 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.

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;

24

- price; and
- product performance in the field.

## Edgar Filing: PUBLICARD INC - Form 10-K

Our ability to develop new products also depends upon the success of our research and development efforts. We may need to devote additional resources to our research and development efforts in the future. We cannot assure you that funds will be available for these expenditures or that these funds 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;
- price;
- product reputation, reliability, quality, performance and customer support;
- product features such as adaptability, functionality and ease of use; and
- 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 could have a material adverse effect on our business and operating results.

Our primary competition currently comes from companies offering closed environment solutions, including small value electronic cash systems and database management solutions, such as Girovend, MARS, Cunninghams, Uniware, Diebold 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 are subject to 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, 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,

## Edgar Filing: PUBLICARD INC - Form 10-K

without any certainty of a sale.

WE MAY BE LIMITED IN OUR USE OF OUR FEDERAL NET OPERATING LOSS CARRYFORWARDS. As of December 31, 2002, we had federal net operating loss carryforwards, subject to review by the Internal Revenue Service, totaling approximately \$65.0 million for federal income tax purposes. The federal net operating loss carryforwards begin to expire in 2005. We do not expect to earn any significant taxable income in the next

25

several years, and may not do so until much later, if ever. A federal net operating loss can generally be carried back two, three or five 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 "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, acquisitions and other transactions in the future, although no assurance can be given that any such offering, acquisition or other transaction will be effected. In addition, the exercise of outstanding 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 virtually all of our available federal net operating loss carryforwards would be effectively unavailable 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 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.



## Edgar Filing: PUBLICARD INC - Form 10-K

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 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 as effectively 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.

We believe that establishing, maintaining and enhancing the Infineer brand name is essential to our business. We filed an application for a United States trademark registration and an application for service mark registration of our name and logo. We are aware of third parties that use marks or names that contain similar sounding words or variations of the "infi" prefix. In July 2002, we received a claim from a third

26

party challenging the use of the Infineer name. We have reached an agreement in principle with this third party, subject to negotiation of definitive documentation, and believe this particular challenge should be resolved. As a result of this claim and other challenges which may occur in the future, we may incur significant expenses, pay substantial damages and be prevented from using the Infineer name. Use of a similar name by third parties may also cause confusion to our clients and confusion in the market, which could decrease the value of our brand and harm our reputation. We cannot assure you that our business would not be adversely affected if we are required to change our name or if confusion in the market did occur.

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 for financial transactions, computer networks, 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 could 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

## Edgar Filing: PUBLICARD INC - Form 10-K

services and performance of our senior management and other key personnel. If we fail to meet our operating and financial objectives this may make it more difficult to retain and reward our senior management and key personnel. 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 and hardware engineers, 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 the future.

Even if we retain our current employees, our management must continually recruit talented professionals in order for our business to grow. 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. Sales outside the U.S. represented approximately 78% of total sales for the year ended December 31, 2002. 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;
- 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.

27

Any of the foregoing could adversely impact the success of our operations. We cannot assure you that such factors will not have a material adverse effect on our future 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.

CHANGES WE MAY NEED OR BE REQUIRED TO MAKE IN OUR INSURANCE COVERAGE MAY EXPOSE US TO INCREASED LIABILITIES AND MAY INTERFERE WITH OUR ABILITY TO RETAIN OR ATTRACT QUALIFIED OFFICERS AND DIRECTORS. We renew or replace various insurance policies on an annual basis, including those that cover directors and officers liability. Given the current climate of rapidly increasing insurance premiums and erosions of coverage, we may need or be required to reduce our coverage and increase our deductibles in order to afford the premiums. To the extent we reduce our coverage and increase our deductibles, our exposure and the exposure of our directors and officers for liabilities that either become excluded from coverage or underinsured will increase. As a result, we may lose

## Edgar Filing: PUBLICARD INC - Form 10-K

or may experience difficulty in attracting qualified directors and officers.

WE ARE SUBJECT TO GOVERNMENT REGULATION. Federal, state and local regulations impose various environmental controls on the discharge of chemicals and gases, which have been used in our past assembly processes and may be used in future 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, could subject us to liabilities and could materially adversely affect our operations.

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. 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 of \$842,000 and Mr. Jay S. Goldsmith of \$842,000. 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 income taxes on

## Edgar Filing: PUBLICARD INC - Form 10-K

such additional payment, equal to the initial payment before such additional payment and we would not be able to deduct these initial or additional 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:

- delisting of our common stock from the Nasdaq SmallCap Market effective March 28, 2003 (see "Our stock is being delisted from the Nasdaq System" above);
- 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;
- our ability to effectively manage our business, including our ability to raise capital;
- variations in our annual or quarterly financial results or those of our competitors;
- general economic conditions, in particular, the technology service sector;
- 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.

29

### ITEM 7A. 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.

## Edgar Filing: PUBLICARD INC - Form 10-K

### Market Risk

We are exposed to market risk primarily through short-term investments and an overdraft facility. Our investment policy calls for investment in short-term, low risk instruments. As of December 31, 2002, short-term investments (principally U.S. Treasury bills) were \$1.1 million. Due to the nature of these investments and amount of the overdraft facility (\$138,000 at December 31, 2002), any decrease in rates would not have a material impact on our financial condition or results of operations.

### Investment Risk

As of December 31, 2002, the carrying value of our investment in TecSec, a privately held company, was \$3.0 million after recording an impairment change of \$2.1 million in the third quarter of 2002. This investment has been accounted for at cost and could be subject to write-downs in future periods if it is determined that the investment is permanently impaired and is not recoverable. TecSec is currently evaluating alternative sources of financing to meet ongoing capital and operating needs. If TecSec is not successful in executing its business plan or in obtaining sufficient capital on acceptable terms or at all, our investment could be further impaired and subject to a significant additional write-down.

### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Company's consolidated financial statements, the report of independent public accountants thereon and related schedules appear beginning on page F-2. See Index to Consolidated Financial Statements on page F-1.

### ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

On June 5, 2002, the Board of Directors of the Company, upon the recommendation of its Audit Committee, decided that effective June 5, 2002 the Company would no longer engage Arthur Andersen LLP ("Arthur Andersen") as the Company's independent public accountants and that as of June 6, 2002 Deloitte & Touche LLP ("Deloitte & Touche"), certified public accountants, would be appointed as the Company's independent public accountants for 2002, subject to ratification by stockholders.

The report of Arthur Andersen on the Company's consolidated financial statements for the fiscal year ended December 31, 2001 contained an unqualified opinion with an emphasis paragraph concerning substantial doubt about the Company's ability to continue as a going concern. The report did not contain any disclaimer or any qualification as to audit scope or accounting principles. The report of Arthur Andersen on the Company's consolidated financials statements for the year ended December 31, 2000 did not contain an adverse opinion or disclaimer of opinion, nor was it qualified or modified as to uncertainty, audit scope or accounting principles.

During the Company's two most recent fiscal years and through June 5, 2002, there were no disagreements with Arthur Andersen on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure which, if not resolved to Arthur Andersen's satisfaction, would have caused it to make reference thereto in connection with its report on the Company's consolidated financial statements for such years; and there were no reportable events as such term is defined in Item 304(a) (1) (v) of Regulation S-K.

Edgar Filing: PUBLICARD INC - Form 10-K

During 2002, there were no disagreements with Deloitte & Touche on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedures which, if not resolved to Deloitte & Touche's satisfaction, would have caused them to make reference to the subject matter in connection with their report on the Company's consolidated financial statements for 2002 and there were no reportable events, as such term is defined in Item 304(a) (1) (v) of Regulation S-K.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information called for by this item is hereby incorporated by reference from the Company's definitive proxy statement to be filed pursuant to Regulation 14A for the 2003 Annual Meeting of Shareholders.

The information with respect to the executive officers of the Company required by this item is set forth in Item 1A of this Form 10-K.

SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), requires the Company's directors and officers and persons who own more than 10 percent of a registered class of the Company's equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission (the "SEC"). Officers, directors and greater than 10% shareholders are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms they file. To the Company's knowledge, based solely upon the Company's review of the copies of such forms received by it during the fiscal year ended December 31, 2002 and representations that no other reports were required, the Company believes that each person who, at any time during such fiscal year, was a director, officer or, to the Company's knowledge, beneficial owner of more than 10% of the Company's common stock complied with all Section 16(a) filing requirements during such fiscal year, except for one late Form 4 report for Clifford Cohn filed on December 31, 2002 relating to several December 2002 transactions.

ITEM 11. EXECUTIVE COMPENSATION

The information called for by this item is hereby incorporated by reference from the Company's definitive proxy statement to be filed pursuant to Regulation 14A for the 2003 Annual Meeting of Shareholders.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table sets forth certain equity compensation plan information for the Company as of December 31, 2002.

	Number of securities to be issued upon exercise	Weighted-average exercise price of	Number of securities remaining available for future issuance under equity compensation plans (exc
--	---	------------------------------------	---

## Edgar Filing: PUBLICARD INC - Form 10-K

Plan category	of outstanding options, warrants and rights (a)	outstanding options, warrants and rights (b)	securities re column (c)
Equity compensation plans approved by security holders	2,939,175	\$1.01	
Equity compensation plans not approved by security holders	363,960	6.31	
Total	3,303,135 =====	\$1.59	

See Note 6 to the Notes to Consolidated Financial Statements for a description of the Company's equity compensation plans.

32

The additional information called for by this item is hereby incorporated by reference from the Company's definitive proxy statement to be filed pursuant to Regulation 14A for the 2003 Annual Meeting of Shareholders.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information called for by this item is hereby incorporated by reference from the Company's definitive proxy statement to be filed pursuant to Regulation 14A for the 2003 Annual Meeting of Shareholders.

### ITEM 14. CONTROLS AND PROCEDURES

With the participation of management, the Company's chief executive officer and chief financial officer evaluated the effectiveness of the Company's disclosure controls and procedures within 90 days of the filing of this report. Based upon this evaluation, the chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures are effective in timely alerting him to material information relating to the Company (including its consolidated subsidiaries) required to be included in the reports that the Company files with the Securities and Exchange Commission.

There were no significant changes in the Company's internal controls or, to the knowledge of the Company's management, in other factors that could significantly affect these controls subsequent to the evaluation date.

33

## PART IV

### ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) Financial Statements, Financial Statement Schedules and Exhibits.

## Edgar Filing: PUBLICARD INC - Form 10-K

- 1) Financial Statements - See accompanying Index to Consolidated Financial Statements, Page F-1.
- 2) Financial Statement Schedules - See accompanying Index to Consolidated Financial Statements, Page F-1.
- 3) Exhibits:
  - 3.1 Amended and Restated Articles of Incorporation, amended and restated through November 2, 1998, of PublicARD. Incorporated by reference to PublicARD's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 1998, dated November 9, 1998.
  - 3.2 By-laws of PublicARD. Incorporated by reference to PublicARD's Annual Report on Form 10-K for the fiscal year ended December 31, 1990, dated March 28, 1991.
  - 4.1 Certificate of Designation, Preferences and Rights of Class A Preferred Stock, First Series. Incorporated by reference from PublicARD's Registration Statement on Form 8-A, dated September 26, 1988.
  - 4.2 Amended and Restated Rights Agreement, dated as of August 7, 1998, between PublicARD and Continental Stock Transfer & Trust Company, as Rights Agent. Incorporated by reference from PublicARD's Current Report on Form 8-K, filed on September 17, 1998.
  - 4.3 Certificate of Designation, Preferences and Rights of Class A Preferred Stock, Second Series as filed with the Department of State of the Commonwealth of Pennsylvania on November 29, 2000. Incorporated by reference from PublicARD's Current Report on Form 8-K filed on December 18, 2000.
  - 4.4 Rights Plan, adopted November 1, 2000. Incorporated by reference from PublicARD's Current Report on Form 8-K filed on December 18, 2000.
  - 10.1 Agreements, dated as of August 1987, between PublicARD and each of Harry I. Freund and Jay S. Goldsmith concerning a change of control of PublicARD. Incorporated by reference from PublicARD's Form 8 Amendment to PublicARD's Quarterly Report on Form 10-Q for the quarter ended September 30, 1987, filed on December 18, 1987.
  - 10.2 PublicARD's 1993 Long Term Incentive Plan. Incorporated by reference from PublicARD's Annual Report on Form 10-K for the year ended December 31, 1993, dated March 29, 1994.
  - 10.3 PublicARD's Non-employee Director Stock Option Plan. Incorporated by reference from PublicARD's Annual Report on Form 10-K for the year ended December 31, 1993, dated March 29, 1994.
  - 10.4 PublicARD's 1999 Stock Option Plan for Non-Employee Directors. Incorporated by reference from PublicARD's Annual Report on Form 10-K for the year ended December 31, 1999, dated March 30, 2000.
  - 10.5 PublicARD's 1999 Long-Term Incentive Plan. Incorporated by reference



Edgar Filing: PUBLICARD INC - Form 10-K

December 31, 1999, dated March 30, 2000.

- 21.1 Subsidiaries of PubliCARD. Filed herewith.
- 23.1 Consent letter from Independent Auditors. Filed herewith.
- 99.1 Certification of periodic report dated March 28, 2003. Filed herewith.
- (b) Reports on Form 8-K  
None.

35

SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) 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 March 24, 2003  
-----

By: /s/ ANTONIO L. DELISE  
-----

Antonio L. DeLise, President,  
Chief Executive Officer, Chief Financial  
Officer and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date March 24, 2003  
-----

By: /s/ ANTONIO L. DELISE  
-----

Antonio L. DeLise, President,  
Chief Executive Officer, Chief Financial  
Officer and Director

Date March 24, 2003  
-----

By: /s/ CLIFFORD B. COHN  
-----

Clifford B. Cohn, Director

Date March 24, 2003  
-----

By: /s/ HARRY I. FREUND  
-----

Harry I. Freund, Chairman and Director

Date March 24, 2003  
-----

By: /s/ JAY S. GOLDSMITH  
-----

Jay S. Goldsmith, Vice Chairman

Date March 24, 2003

By: /s/ L. G. SCHAFFRAN

Edgar Filing: PUBLICARD INC - Form 10-K

-----  
Date March 24, 2003  
-----

-----  
By: /s/ EMIL VOGEL  
-----

L. G. Schafran, Director

Emil Vogel, Director

36

CERTIFICATION

I, Antonio L. DeLise, as the President, Chief Executive Officer and Chief Financial Officer of PubliCARD, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of PubliCARD, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and I have:
  - (a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this annual report is being prepared;
  - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
  - (c) Presented in this annual report my conclusions about the effectiveness of the disclosure controls and procedures based on my evaluation as of the Evaluation Date;
5. I have disclosed, based on my most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - (a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of my most recent evaluation, including

Edgar Filing: PUBLICARD INC - Form 10-K

any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 28, 2003

/s/ Antonio L. DeLise

-----  
Antonio L. DeLise  
President, Chief Executive Officer,  
Chief Financial Officer and Secretary

37

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE

Financial Statements

Independent auditors' report-- Deloitte & Touche LLP	F-2
Report of independent public accountants --Arthur Andersen LLP	F-3
Consolidated balance sheets as of December 31, 2002 and 2001	F-4
Consolidated statements of operations for the years ended December 31, 2002, 2001 and 2000	F-5
Consolidated statements of shareholders' equity (deficit) for the years ended December 31, 2002, 2001 and 2000	F-6 and F-7
Consolidated statements of cash flows for the years ended December 31, 2002, 2001 and 2000	F-8
Notes to consolidated financial statements	F-9 through F-26
Schedule	
-----	
Independent auditors' report on schedule--Deloitte Touche LLP	F-27
Report of independent public accountants on schedule--Arthur Andeersen LLP	F-28
Schedule II - Valuation and qualifying accounts	F-29

All other schedules required by Regulation S-X have been omitted because they are not applicable or because the required information is included in the financial statements or notes thereto.

F-1

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

INDEPENDENT AUDITORS' REPORT

## Edgar Filing: PUBLICARD INC - Form 10-K

To the Board of Directors and Shareholders of  
PubliCARD, Inc.  
New York, New York

We have audited the accompanying consolidated balance sheet of PubliCARD, Inc. and subsidiary companies (the "Company") as of December 31, 2002, and the related consolidated statements of operations, shareholders' equity (deficit), and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Company as of December 31, 2001 and for each of the years in the two-year period then ended, before the inclusion of the transitional disclosures relating to Goodwill and Intangible Assets, as described in Note 1 of the notes to the consolidated financial statements, were audited by other auditors who have ceased operations. Those auditors expressed an unqualified opinion on those financial statements in their report dated March 20, 2002.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2002 consolidated financial statements present fairly, in all material respects, the financial position of PubliCARD, Inc. and subsidiary companies as of December 31, 2002, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 of the notes to the consolidated financial statements, the Company changed its method of accounting for goodwill and other intangible assets to conform to Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets ("SFAS 142").

As discussed above, the consolidated financial statements of PubliCARD, Inc. and subsidiary companies as of December 31, 2001, and for each of the years in the two-year period then ended, were audited by other auditors who have ceased operations. As described in Note 1, these consolidated financial statements have been revised to include the transitional disclosures required by SFAS 142, which was adopted by the Company as of January 1, 2002. Our audit procedures with respect to the disclosures in Note 1 with respect to 2001 and 2000 included (1) comparing the previously reported net loss to the previously issued financial statements and the adjustments to reported net loss representing amortization expense recognized in those periods related to goodwill, to the Company's underlying analysis obtained from management, and (2) testing the mathematical accuracy of the reconciliation of adjusted net loss to reported net loss and the related loss-per-share amounts. In our opinion, the disclosures for 2001 and 2000 in Note 1 are appropriate. However, we were not engaged to audit, review, or apply any procedures to the 2001 and 2000 consolidated financial statements of the Company other than with respect to such disclosures and, accordingly, we do not express an opinion or any other form of assurance on the 2001 and 2000 consolidated financial statements taken as a whole.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has experienced recurring losses from operations, a substantial decline in working capital and negative cash flows from operations, and requires additional capital to meet its obligations,

## Edgar Filing: PUBLICARD INC - Form 10-K

which raises substantial doubt about its ability to continue as a going concern. Management's plans concerning these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ DELOITTE & TOUCHE LLP

New York, New York  
March 24, 2003

F-2

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

PublicARD, Inc. dismissed Arthur Andersen LLP on June 5, 2002, and subsequently engaged Deloitte & Touche LLP as its independent auditors. The predecessor auditors' report appearing below is a copy of Arthur Andersen LLP's previously issued opinion dated March 20, 2002. Since PublicARD, Inc. is unable to obtain a manually signed audit report, a copy of Arthur Andersen LLP's most recently signed and dated report has been included below to satisfy filing requirements, as permitted under Rule 2-02(e) of Regulation S-X.

To the Shareholders of PublicARD, Inc.:

We have audited the accompanying consolidated balance sheets of PublicARD, Inc. (a Pennsylvania corporation) and subsidiary companies as of December 31, 2001 and 2000, and the related consolidated statements of income (loss), shareholders' equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PublicARD, Inc. and subsidiary companies as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has incurred operating losses and requires additional capital to meet its obligations and accomplish the Company's business plan, which raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Edgar Filing: PUBLICARD INC - Form 10-K

/s/ Arthur Andersen LLP

Stamford, Connecticut

March 20, 2002

F-3

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEETS  
DECEMBER 31, 2002 AND 2001

	2002 ----	2001 ----
	(in thousands except share data)	
ASSETS		
Current assets:		
Cash, including short-term investments of \$1,138 and \$4,199 in 2002 and 2001, respectively	\$ 1,290	\$ 4,479
Trade receivables, less allowance for doubtful accounts of \$103 and \$216 in 2002 and 2001, respectively	853	1,410
Inventories	885	557
Prepaid insurance and other	375	770
	-----	-----
Total current assets	3,403	7,216
	-----	-----
Equipment and leasehold improvements, net	379	596
Goodwill and intangibles	862	2,803
Other assets	3,295	6,782
	-----	-----
	\$ 7,939	\$ 17,397
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Trade accounts payable and overdraft	\$ 1,269	\$ 1,206
Accrued liabilities	2,682	3,379
	-----	-----
Total current liabilities	3,951	4,585
Other non-current liabilities	4,990	5,328
	-----	-----
Total liabilities	8,941	9,913
	-----	-----
Commitments and contingencies (Note 7)		
Shareholders' equity (deficit):		
Class A Preferred Stock, Second Series, no par value: 1,000 shares authorized; 765 and 780 issued and outstanding as of December 31, 2002 and 2001, respectively	3,825	3,900

## Edgar Filing: PUBLICARD INC - Form 10-K

Common shares, \$0.10 par value: 40,000,000 shares authorized; 24,190,902 and 24,153,402 shares issued and outstanding as of December 31, 2002 and 2001, respectively	2,419	2,415
Additional paid-in capital	107,169	107,098
Accumulated deficit	(112,024)	(104,831)
Other comprehensive loss	(2,391)	(1,098)
	-----	-----
Total shareholders' equity (deficit)	(1,002)	7,484
	-----	-----
	\$ 7,939	\$ 17,397
	=====	=====

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

F-4

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

	2002 ----	2001 ----	2000 ----
(in thousands except share data)			
Net sales	\$ 4,605	\$ 5,652	\$ 5,54
	-----	-----	-----
Cost of sales	2,455	2,875	2,91
Inventory adjustment	--	1,661	-
	-----	-----	-----
Gross margin	2,150	1,116	2,63
	-----	-----	-----
Operating expenses:			
General and administrative	3,235	4,625	6,66
Sales and marketing	1,877	3,413	7,56
Product development	605	2,442	4,36
Stock compensation expense	--	86	1,11
Amortization of goodwill and intangibles	576	1,824	2,63
Impairment of goodwill and intangibles	1,365	--	-
Repositioning charge	--	5,656	-
	-----	-----	-----
	7,658	18,046	22,34
	-----	-----	-----
Loss from operations	(5,508)	(16,930)	(19,71)
	-----	-----	-----
Other income (expenses):			
Interest income	71	476	93
Interest expense	(39)	(65)	(10)
Cost of retirement benefits - non-operating	(795)	(788)	(81)
Write-down of minority investment	(2,068)	--	-
Other income	80	136	1

Edgar Filing: PUBLICARD INC - Form 10-K

	-----	-----	-----
	(2,751)	(241)	3
	-----	-----	-----
Loss from continuing operations	(8,259)	(17,171)	(19,67
Income from discontinued operations	1,066	2,350	4,27
Net loss	\$ (7,193)	\$ (14,821)	\$ (15,40
	=====	=====	=====
Basic and diluted earnings (loss) per common share:			
Continuing operations	\$ (.34)	\$ (.71)	\$ (.8
Discontinued operations	.04	.10	.1
	-----	-----	-----
	\$ (.30)	\$ (.61)	\$ (.6
	=====	=====	=====
Weighted average common shares outstanding	24,179,364	24,188,325	23,295,12
	=====	=====	=====

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

F-5

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (DEFICIT)  
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

	Class A Preferred Stock		Common Shares		Add
	Shares Issued	Amount	Shares Issued	Amount	P C
	-----	-----	-----	-----	---
	(in thousands except share data)				
Balance - December 31, 1999	--	\$ --	\$ 26,191,189	\$ 2,619	\$
Shares issued:					
Stock option plans	--	--	1,177,501	118	
Private placement	790	3,950	525,000	53	
Business acquisitions	--	--	66,333	7	
Pension plan contribution	--	--	115,000	11	
Employment and separation agreements	--	--	251,500	25	
Amortization of unearned compensation	--	--	--	--	
Cancellation of treasury shares	--	--	(4,089,121)	(409)	
Net loss	--	--	--	--	
	-----	-----	-----	-----	-----
Balance - December 31, 2000	790	3,950	24,237,402	2,424	



Edgar Filing: PUBLICARD INC - Form 10-K

Conversion of preferred stock	(10)	(50)	25,000	2
Private placement costs	--	--	--	--
Repurchase of common shares	--	--	(109,000)	(11)
Amortization of unearned compensation	--	--	--	--
Comprehensive loss:				
Net loss	--	--	--	--
Foreign currency translation adjustment	--	--	--	--
Minimum pension liability	--	--	--	--
	-----	-----	-----	-----
Total comprehensive loss				
Balance - December 31, 2001	780	\$ 3,900	24,153,402	\$ 2,415
	=====	=====	=====	=====

	Accumulated Deficit -----	Other Comprehensive Loss -----	Treasury Shares(1) -----	Unearned Compensa tion -----
	(in thousands except share data)			
Balance - December 31, 1999	\$ (74,610)	\$ --	(8,649)	\$ (437)
	-----	-----	-----	-----
Shares issued:				
Stock option plans	--	--	(1,923)	--
Private placement	--	--	--	--
Business acquisitions	--	--	--	--
Pension plan contribution	--	--	--	--
Employment and separation agreements	--	--	--	--
Amortization of unearned compensation	--	--	--	351
Cancellation of treasury shares	--	--	10,572	--
Net loss	(15,400)	--	--	--
	-----	-----	-----	-----
Balance - December 31, 2000	(90,010)	--	--	(86)
Conversion of preferred stock	--	--	--	--
Private placement costs	--	--	--	--
Repurchase of common shares	--	--	--	--
Amortization of unearned compensation	--	--	--	86
Comprehensive loss:				
Net loss	(14,821)	--	--	--
Foreign currency translation adjustment	--	(197)	--	--
Minimum pension liability	--	(901)	--	--
	-----	-----	-----	-----
Total comprehensive loss				
Balance - December 31, 2001	\$ (104,831)	\$ (1,098)	\$ --	\$ --
	=====	=====	=====	=====

(continued on next page)

Edgar Filing: PUBLICARD INC - Form 10-K

F-6

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (DEFICIT)  
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

	Class A Preferred Stock		Common Shares		Add P C
	Shares Issued	Amount	Shares Issued	Amount	
(in thousands except share data)					
Balance - December 31, 2001	780	\$ 3,900	24,153,402	\$2,415	\$10
Conversion of preferred stock	(15)	(75)	37,500	4	
Comprehensive loss:					
Net loss	--	--	--	--	
Foreign currency translation adjustment	--	--	--	--	
Minimum pension liability	--	--	--	--	
Total comprehensive loss					
Balance - December 31, 2002	765	\$ 3,825	24,190,902	\$2,419	\$10

	Accumulated Deficit	Other Comprehensive Loss	Treasury Shares(1)	Unearned Compensa tion
	-----	-----	-----	-----
(in thousands except share data)				
Balance - December 31, 2001	\$(104,831)	\$(1,098)	\$ --	\$ --
Conversion of preferred stock	--	--	--	--
Comprehensive loss:				
Net loss	(7,193)	--	--	--
Foreign currency translation adjustment	--	112	--	--
Minimum pension liability	--	(1,405)	--	--
Total comprehensive loss				
Balance - December 31, 2002	\$(112,024)	\$(2,391)	\$ --	\$ --

(1) Represents common shares held in treasury of 3,725,024 at December 31, 1999

## Edgar Filing: PUBLICARD INC - Form 10-K

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

F-7

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

	2002	2001	2000
	-----	-----	-----
	(in thousands)		
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net loss	\$ (7,193)	\$ (14,821)	\$ (15,000)
Adjustments to reconcile net loss to net cash used in operating activities:			
Gain from discontinued operations	(1,066)	(2,350)	(4,000)
Write-down of minority investment	2,068	--	--
Amortization of goodwill and intangibles	576	1,824	2,000
Impairment of goodwill and intangibles	1,365	--	--
Stock compensation expense	--	86	1,000
Depreciation	205	308	--
Repositioning charge and inventory adjustment	--	7,317	--
Changes in assets and liabilities	(1,040)	(5,034)	(6,000)
	-----	-----	-----
Net cash used in operating activities	(5,085)	(12,670)	(21,000)
	-----	-----	-----
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Investment in minority owned affiliates	--	(5)	(5)
Capital expenditures	(28)	(83)	(1)
Proceeds from discontinued operations and sale of fixed assets	1,865	223	21
Other	47	11	--
	-----	-----	-----
Net cash provided by investing activities	1,884	146	15
	-----	-----	-----
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Proceeds from private placement of Class A Preferred Stock	--	(43)	3
Proceeds from private placement of common shares	--	--	--
Issuance of common shares pursuant to stock option exercises	--	--	1
Repayment of notes payable from discontinued operations	--	--	--
	-----	-----	-----
Net cash (used in) provided by financing activities	--	(43)	5
	-----	-----	-----
Effect of exchange rate changes on cash and cash equivalents	12	(3)	--
	-----	-----	-----
Net decrease in cash	(3,189)	(12,570)	(1)
Cash - beginning of period	4,479	17,049	18
	-----	-----	-----
Cash - end of period	\$ 1,290	\$ 4,479	\$ 17
	=====	=====	=====

## Edgar Filing: PUBLICARD INC - Form 10-K

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

F-8

### 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 (the "Board"), 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 adopted a plan of disposition pursuant to which the Company divested its non-core operations. See Note 9 for a discussion on the disposition plan.

In July 2001, after evaluating the timing of potential future revenues, PublicARD's Board decided to shift the Company's strategic focus. While the Board remained confident in the long-term prospects of the smart card business, the timing of public sector and corporate initiatives in wide-scale, broadband environments utilizing the Company's smart card reader and chip products had become more uncertain. Given the lengthened time horizon, the Board did not believe it would be prudent to continue to invest the Company's current resources in the ongoing development and marketing of these technologies. Accordingly, the Board determined that shareholders' interests will be best served by pursuing strategic alliances with one or more companies that have the resources to capitalize more fully on the Company's smart card reader and chip-related technologies. In connection with this shift in the Company's strategic focus, workforce reductions and other measures were implemented to achieve cost savings. See Note 10 for a discussion on the repositioning charge associated with this action.

At present, PublicARD's sole operating activities are conducted through its Infineer Ltd. subsidiary ("Infineer"), which designs smart card solutions for educational and corporate sites. The Company's future plans revolve around a potential acquisition strategy that would focus on businesses in areas outside the high technology sector while continuing to support the expansion of the Infineer business. However, the Company will not be able to implement such plans unless it is successful in obtaining funding, as to which no assurance can be given.

###### LIQUIDITY AND GOING CONCERN CONSIDERATIONS

These consolidated financial statements contemplate the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred operating losses, a substantial decline in working capital and negative cash flow from operations for the years 2002, 2001 and 2000. The Company has also experienced a substantial reduction in its cash and short term investments, which declined from \$17.0 million at December 31, 2000, to \$4.5 million at December 31, 2001 and to \$1.3 million at December 31, 2002. The

## Edgar Filing: PUBLICARD INC - Form 10-K

Company also had a working capital deficiency of \$548,000 and an accumulated deficit of \$112.0 million at December 31, 2002.

If the distress termination of the Company's defined benefit pension plan for which the Company has applied is completed (see Note 5), the Company's 2003 funding requirements to the plan could be eliminated, in which case management believes that existing cash and short term investments may be sufficient to meet the Company's operating and capital requirements at the currently anticipated levels through December 31, 2003. However, additional capital will be necessary in order to operate beyond December 2003 and to fund the current business plan and other obligations. While the Company is actively considering various funding alternatives, the Company has not secured or entered into any arrangements to obtain additional funds. There can be no assurance that the Company will eliminate the 2003 funding requirements for the defined benefit pension plan or be able to obtain additional funding on acceptable terms or at all. If the Company cannot raise additional capital to continue

F-9

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

its present level of operations it may not be able to meet its obligations, take advantage of future acquisition opportunities or further develop or enhance its product offering, any of which could have a material adverse effect on its business and results of operations and could lead the Company to seek bankruptcy protection. These conditions raise substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of PubliCARD and its wholly-owned subsidiaries. All intercompany transactions are eliminated in consolidation.

#### SHORT-TERM INVESTMENTS

Short-term investments consist of certain liquid instruments with original maturities of three months or less including U.S. Treasury obligations and money market funds.

#### INVENTORIES

Inventories are stated at lower of cost (first-in, first-out method) or market. The Company periodically evaluates the need to record adjustments for impairment of inventory. 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 management's estimates related to the Company's production schedules, customer demand, possible alternative uses and the ultimate realization of potentially excess inventory. Inventories at December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----
Raw materials and supplies	\$154	\$389
Work-in-process	21	37

## Edgar Filing: PUBLICARD INC - Form 10-K

Finished goods	710	131
	----	----
	\$885	\$557
	=====	=====

### DEPRECIATION AND AMORTIZATION

Equipment and leasehold improvements are stated at cost. Improvements and replacements are capitalized, while expenditures for maintenance and repairs are charged to expense as incurred. Depreciation for equipment is computed using the straight-line method over estimated useful lives of three to five years. Amortization for leasehold improvements is computed using the lesser of the estimated useful life or the life of the lease. Equipment and leasehold improvements at December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----
Equipment, furniture and fixtures	\$ 899	\$931
Leasehold improvements	224	237
Accumulated depreciation and amortization	(744)	(572)
	-----	-----
	\$ 379	\$596
	=====	=====

Depreciation and amortization expense was \$205,000, \$308,000 and \$314,000 in 2002, 2001 and 2000, respectively.

### GOODWILL AND INTANGIBLES

Goodwill is the excess of the purchase price and related costs over the value assigned to the net tangible and intangible assets relating to the November 1999 acquisition of Infineer. Through December 31, 2001, goodwill had been amortized over a five year life. Effective January 1, 2002, the Company adopted Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). In accordance with the guidelines of this statement, goodwill and

F-10

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

indefinite lived intangible assets are no longer amortized but will be assessed for impairment on at least an annual basis. SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives and reviewed for impairment. The Company performed an initial review for impairment of goodwill as of January 1, 2002 and determined that no impairment existed at that date. The Company determined the fair value of its sole reporting unit primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for

## Edgar Filing: PUBLICARD INC - Form 10-K

several entities with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor.

The Company performed its annual goodwill impairment test in the fourth quarter of 2002 and determined that goodwill had been impaired. The Company determined the fair value primarily using two approaches: a market approach technique and a discounted cash flow valuation technique. The market approach relied primarily on the implied fair value using a multiple of revenues for an entity with comparable operations and economic characteristics. Significant assumptions used in the discounted cash valuation included estimates of future cash flows, future short-term and long-term growth rates and estimated cost of capital for purposes of arriving at a discount factor. Based on comparing the values derived from the two techniques to the carrying value of the reporting unit, the Company recorded a goodwill impairment loss of \$364,000 in the fourth quarter of 2002. The Company attributes the impairment loss to the value of a comparable entity that was sold in a transaction in late 2002, the significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to a continued overall decline in technology spending and a shortage of capital available to invest in the reporting unit. On an ongoing basis, the Company expects to perform its annual impairment test during the fourth quarter absent any interim impairment indicators.

The changes in the carrying value of goodwill for the year ended December 31, 2002 was as follows (in thousands):

	2002
	----
Balance, December 31, 2001	\$ 1,146
Impairment loss	(364)
	-----
Balance, December 31, 2002	\$ 782
	=====

Amortization of goodwill for 2001 and 2000 was \$1.1 million and \$1.7 million, respectively. In 2001, the Company wrote-off \$3.3 million of goodwill associated with the July 2001 repositioning action. See Note 10.

Intangible assets consist of completed technology identified as of the Infeiner acquisition date and are amortized over a five year life. Long-lived assets and certain identifiable intangible assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of any impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the net realizable of the asset. In the fourth quarter of 2002, the Company determined that its intangible assets had been impaired and recorded an impairment loss of \$1.0 million. The Company attributes the impairment loss to the significant 2002 operating loss for the reporting unit and lower forecasted revenue growth due to a continued overall decline in technology spending and a shortage of capital available to invest in the reporting unit.

# Edgar Filing: PUBLICARD INC - Form 10-K

## PUBLICARD, INC. AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The gross carrying amount and accumulated amortization of intangible assets at December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----
Gross carrying amount	\$ 2,882	\$ 2,882
Impairment loss	(1,001)	--
	-----	-----
Adjusted carrying amount	1,881	2,882
Accumulated amortization	(1,801)	(1,225)
	-----	-----
	\$ 80	\$ 1,657
	=====	=====

Amortization of intangibles for 2002, 2001 and 2000 was \$576,000, \$746,000 and \$916,000, respectively. In 2001, the Company wrote-off \$822,000 of intangibles associated with the July 2001 repositioning action. See Note 10. The estimated annual amortization expense for intangibles is \$40,000 for each of the years 2003 and 2004.

#### REVENUE RECOGNITION AND ACCOUNTS RECEIVABLE

Revenue from product sales and technology and software license fees is recorded upon shipment if a signed contract exists, the fee is fixed and determinable, the collection of the resulting receivable is probable and the Company has no obligation to install the product or solution. If the Company is responsible for installation, revenue from product sales and license fees is recognized upon client acceptance or "go live" date. Revenue from maintenance and support fees is recognized ratably over the contract period. Provisions are recorded for estimated warranty repairs and returns at the time the products are shipped. Should changes in conditions cause management to determine that revenue recognition criteria are not met for certain future transactions, revenue recognized for any reporting period could be adversely affected.

The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's credit worthiness. The Company continually monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that it has identified. While such credit losses have historically been within management's expectations and the provisions established, there is no assurance that the Company will continue to experience the same credit loss rates as in the past.

#### STOCK-BASED COMPENSATION

SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), requires that an entity account for employee stock-based compensation under a fair value based method. However, SFAS No. 123 also allows an entity to continue to measure compensation cost using the intrinsic value method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25"). The Company continues to account for



## Edgar Filing: PUBLICARD INC - Form 10-K

employee stock-based compensation using the intrinsic value based method and is required to make pro forma disclosures of net income (loss) and related per share amounts as if the fair value based method of accounting under SFAS No. 123 had been applied. Restricted stock or stock awards are recorded as compensation expense over the vesting period, if any, based on the market value on the date of grant.

At December 31, 2002, the Company had four fixed stock-based compensation plans, which are described more fully in Note 6. The exercise price of each option granted pursuant to these plans is equal to the market price of the Company's common stock on the date of grant. Accordingly, pursuant to APB Opinion No. 25, no compensation cost has been recognized for such grants. Had compensation cost been determined based on the fair value at the grant dates for such awards consistent with the method prescribed by SFAS No. 123, the

F-12

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Company's net income and earnings per share would have been as follows (in thousands except per share data):

	2002 ----	2001 ----	2000 ----
Net loss, as reported	\$(7,193)	\$(14,821)	\$(15,400)
Deduct: Total stock-based compensation expense determined under fair value based method	(172)	(1,301)	(5,711)
	-----	-----	-----
Pro forma net loss	\$(7,365)	\$(16,122)	\$(21,111)
	=====	=====	=====
Loss per share:			
As reported	\$ (.30)	\$ (.61)	\$ (.66)
	=====	=====	=====
Pro forma	\$ (.30)	\$ (.67)	\$ (.91)
	=====	=====	=====

For purposes of the pro forma disclosure, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. The weighted average assumptions used to estimate the value of the options included in the pro forma amounts and the weighted average estimated fair value of an option granted are as follows:

2002 ----	2001 ----	2000 ----
--------------	--------------	--------------

## Edgar Filing: PUBLICARD INC - Form 10-K

Expected option term (years)	5.0	7.85	5.0
Expected volatility	75.0%	85.0%	82.2%
Risk-free interest rate	3.5%	6.2%	5.8%
Weighted average fair value per option	\$ .16	\$ .31	\$ 3.60

### USE OF ESTIMATES

The preparation of these financial statements required the use of certain estimates by management in determining the Company's assets, liabilities, revenues and expenses. Certain of our accounting policies require the application of significant judgment by management in selecting the appropriate assumptions for calculating financial estimates. By their nature these judgments are subject to an inherent degree of uncertainty. The Company considers certain accounting policies related to revenue recognition, estimates of reserves for receivables and inventories, valuation of investments, goodwill and intangibles and pension accounting to be critical policies due to the estimation processes involved. While all available information has been considered, actual amounts could differ from those reported.

### 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 year. 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 the same as basic net income (loss) per share since the effect of stock options, warrants and convertible preferred stock were anti-dilutive.

### FOREIGN CURRENCY TRANSLATION

Assets and liabilities of the Company's foreign affiliate are translated at current exchange rates, while revenue and expenses are translated at average rates prevailing during the year. The translation adjustment recorded for 2000 did not have a material effect on the Company's financial statements.

F-13

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### CONCENTRATION OF CREDIT RISK

The carrying amount of financial instruments including cash and short-term investments, accounts receivable and accounts payable approximated fair value as of December 31, 2002, because of the relatively short maturity of these instruments. The Company maintains all of its cash and short-term investments with high-credit quality financial institutions. For the year ended December 31, 2002, one customer represented approximately 10% of sales. Amounts due from a second customer represented approximately 12% of the accounts receivable balance as of December 31, 2002.

#### RESEARCH AND DEVELOPMENT AND SOFTWARE DEVELOPMENT COSTS

Research and development costs are expensed as incurred. In accordance with SFAS No. 86 "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed", the Company capitalizes eligible computer software costs upon achievement of technological feasibility subject to net realizable value considerations. Through December 31, 2002, such costs eligible for capitalization were insignificant. Accordingly, all such costs have been

## Edgar Filing: PUBLICARD INC - Form 10-K

charged to product development expenses.

### INCOME TAXES

The Company follows SFAS No. 109, "Accounting for Income Taxes" ("SFAS No. 109"). Under the asset and liability method of SFAS No. 109, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Since the Company has no recent history of profits, management cannot assess the likelihood that the future benefit of these losses will be recognized. Thus, a full valuation allowance has been recorded.

### RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued SFAS No. 141, "Business Combinations" ("SFAS No. 141"). SFAS No. 141 addresses financial accounting and reporting for business combinations. This new statement requires that all business combinations be accounted for using one method (the purchase method), intangible assets be recognized apart from goodwill if they meet certain criteria and disclosure of the primary reasons for a business combination and the allocation of the purchase price paid to the assets acquired and liabilities assumed by major balance sheet caption. The provisions of this statement apply to all business combinations initiated after June 30, 2001.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). SFAS No. 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets. Under this new statement, goodwill and intangible assets that have indefinite useful lives will not be amortized, but rather will be tested at least annually for impairment, or earlier if circumstances or events indicate that impairment may have occurred, based on the specific guidance of this statement. This may result in future write-downs or the write-off of such assets. In addition, this statement requires disclosure of information about goodwill and other intangible assets in the years subsequent to their acquisition that was not previously required. The provisions of this statement are required to be applied starting with fiscal years beginning after December 15, 2001. However, goodwill and intangible assets acquired after June 30, 2001 were subject immediately to the non-amortization and amortization provisions of this statement. The Company adopted this statement on January 1, 2002. The Company completed the initial impairment test in the first quarter of 2002 which did not result in an impairment of goodwill. The provisions of SFAS No. 142 are effective for periods after adoption and retroactive application is not permitted. Therefore, the historical results of periods prior to 2002 in the Company's Consolidated Statements of Operations do not reflect the effect of SFAS No. 142 and, accordingly, the 2001 and 2000 results included goodwill amortization expense of \$1.1 million and \$1.7 million, respectively. Excluding goodwill amortization, the pro forma net loss for 2001 and 2000 was \$13.7 million and \$13.7 million or \$.57 and \$.59 per share, respectively.

F-14

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"). SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of", and

## Edgar Filing: PUBLICARD INC - Form 10-K

the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions", for the disposal of a segment of a business. This statement also amends ARB No. 51, "Consolidated Financial Statements", to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary. The provisions of this statement are required to be applied starting with fiscal years beginning after December 15, 2001. The Company adopted SFAS No. 144 in the first quarter of fiscal 2002, which did not have an effect on the Company's results of operations or financial position.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS No. 146"). SFAS No. 146 will supersede Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)". SFAS No. 146 requires that costs associated with an exit or disposal plan be recognized when incurred rather than at the date of a commitment to an exit or disposal plan. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The Company does not believe that the adoption of SFAS No. 146 will have a material effect on its Consolidated Financial Statements.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure". SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation", to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock based employee compensation and the effect of the method used on reported results. The provisions of SFAS No. 148 are effective for financial statements for fiscal years and interim periods ending after December 15, 2002. The disclosure provisions of SFAS No. 148 have been adopted by the Company (see above). SFAS No. 148 did not require the Company to change to the fair value based method of accounting for stock-based compensation.

### NOTE 2 - INVESTMENTS

In December 2000, the Company acquired an ownership interest in TecSec, Incorporated, a Virginia corporation ("TecSec"), for \$5.1 million. TecSec develops and markets encryption products and solutions, which are designed to enable the next generation information security for the enterprise, multi-enterprise e-business and other markets. The TecSec investment, amounting to a 5% ownership interest on a fully diluted basis, has been accounted for at cost. The Company has certain anti-dilutive rights whereby its ownership interest may be increased following contributions of additional third-party capital. For the year ended December 31, 2002, TecSec reported unaudited revenues of approximately \$1.4 million, a net loss of \$6.6 million and a decrease in cash of \$5.2 million. TecSec also reported an unaudited deficit in shareholders equity of \$1.9 million and cash of \$64,000 at December 31, 2002. The Company believes that the investment in TecSec has been impaired and a charge of \$2.1 million, which is included in "Other expense (income)", was recorded in the third quarter of 2002. The Company attributes the impairment to a general decline in valuations of technology entities, the difficulties in raising capital and TecSec's recurring operating losses. TecSec is currently evaluating alternative sources of financing to meet ongoing capital and operating needs. If TecSec is not successful in executing its business plan or in obtaining sufficient capital on acceptable terms or at all, the Company's investment in TecSec could be further impaired and subject to an additional significant write-down.

# Edgar Filing: PUBLICARD INC - Form 10-K

F-15

## PUBLICARD, INC. AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In conjunction with the decision to exit the smart card reader and chip business, in September 2001, the Company formed a new minority-owned affiliate, Mako Technologies LLC ("Mako"), to market its smart card reader and chip technologies. The Company contributed certain inventories and equipment valued at \$238,000, in exchange for a 31% fully diluted ownership interest in Mako. The Company also granted a license of its reader and chip technology to Mako in exchange for royalties based on sales over the next two years. After reducing headcount and reassessing business potential, a decision was made in April 2002 to liquidate Mako and terminate the license agreement. Pending the final wind-down of this venture, the Company wrote-off the entire investment in Mako in 2002. During 2002, the Company also realized proceeds of \$224,000 from the sale of smart card reader and chip inventory, which had been previously written-off. The Mako write-off and inventory proceeds are reflected in "Other (expense) income".

#### NOTE 3 - SHAREHOLDERS' EQUITY

On December 6, 2000, the Company completed the private placement of 525,000 shares of common stock and 790 shares of Class A Preferred Stock, Second Series ("Class A Preferred Stock"), a newly designated series of convertible preferred stock, resulting in aggregate proceeds of \$5.0 million to PublicARD. The securities were sold to institutional investors and other accredited investors in the U.S. and Europe. Each share of Class A Preferred Stock is convertible into 2,500 shares of common stock. Therefore, the shares of common stock issued plus the shares of common stock issuable upon conversion of the Class A Preferred Stock aggregate 2.5 million common shares. The proceeds from the private placement were used to acquire the ownership interest in TecSec. In August 2001 and April 2002, 10 shares and 15 shares of Class A Preferred Stock were converted into 25,000 shares and 37,500 shares, respectively, of PublicARD's common stock.

In connection with the December 2000 private placement, the Company issued 100 rights equally to the participants in the private placement. These rights entitle the participating holders of common stock and Class A Preferred stock to receive an aggregate of ten percent of any increase in value of the TecSec investment realized by the Company. The Company performed an internal valuation of the participation rights and concluded their value on the issuance date to be de minimus.

In June 2001, the Company repurchased 109,000 shares of common stock pursuant to an incentive award agreement related to the disposition of certain assets.

In December 2000, the Company returned 4.1 million shares of treasury stock to the status of unissued shares of common stock. An amount was charged to common shares at par value with the remainder being charged to additional paid-in capital.

On August 9, 1988, the Company declared a dividend of one right ("Right") for each outstanding share of its common stock. Each Right entitles the holder to purchase one one-hundredth of a share of a new series of Class A Preferred Stock, First Series, at an exercise price of \$7.50, subject to adjustment to prevent dilution. The Rights become exercisable 10 days after a person or group acquires 20% or more of the Company's common stock or announces a tender or

## Edgar Filing: PUBLICARD INC - Form 10-K

exchange offer for 30% or more of the Company's common stock. If, after the Rights become exercisable, the Company is party to a merger or similar business combination transaction, each Right not held by a party to such transaction may be used to purchase common stock having a market value of two times the exercise price. The Rights, which have no voting power, may be redeemed by the Company at \$.01 per Right. In July 1998, the Company's Board of Directors approved the extension of the rights plan to August 8, 2008.

F-16

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 - INCOME TAXES

As of December 31, 2002, approximately \$65 million of U.S. tax loss carryforwards (subject to review by the Internal Revenue Service), expiring from 2005 through 2022, were available to offset future taxable income. The carryforwards expire as follows (in thousands):

YEAR ENDING DECEMBER 31, -----	AMOUNT -----
2005	\$ 7,000
2006	2,000
2007	4,000
2008	5,000
2009	2,000
2010 - 2022	45,000
	-----
	\$ 65,000
	=====

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. If such change in ownership were to occur, management estimates that virtually all of the available net operating loss carryforwards would be unavailable to reduce its income tax liability. Furthermore, the extent of the actual future use of the net operating loss carryforwards is subject to inherent uncertainty, because it depends on the amount of otherwise taxable income the Company may earn. No assurance can be given that the Company will have sufficient taxable income in future years, if any, to use the net operating losses before they would otherwise expire.

No income tax provision or benefit was recognized in 2002, 2001 and 2000 because the tax benefit associated with the Company's operating losses (35% federal tax rate and 7% state tax rate) were offset in full by an increase in the valuation allowance.

The components of net deferred taxes are as follows (in thousands):

Edgar Filing: PUBLICARD INC - Form 10-K

	2002 ----	2001 ----
Net operating loss carryforward	\$ 22,594	\$ 29,985
Pension expense	1,155	1,305
TecSec investment	724	--
Discontinued operations	35	303
Other, net	126	243
	-----	-----
	24,634	31,836
Less valuation allowance	(24,634)	(31,836)
	-----	-----
Net deferred taxes	\$ --	\$ --
	=====	=====

NOTE 5 - EMPLOYEE BENEFITS

The Company maintains a 401(k) plan for all of the Company's U.S. employees. The assets of the Company's 401(k) plan are held by an outside fund manager and are invested in accordance with the instructions of the individual plan participants. The Company's matching contributions totaled \$14,000, \$68,000 and \$86,000 in 2002, 2001 and 2000, respectively.

F-17

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company sponsors a defined benefit pension plan (the "Plan") that was frozen in 1993. The assets of the Plan are managed by an outside trustee and invested primarily in equity and fixed income securities. PublicARD common stock represented less than 1% of plan assets as of December 31, 2002. The Company's present funding policy is to contribute amounts sufficient to meet the minimum funding requirements as set forth in employee benefit and tax laws. Contributions to the Plan were \$1.1 million, \$1.1 million and \$1.2 million in fiscal 2002, 2001 and 2000, respectively. For 2003, the minimum required contributions are expected to be \$1.5 million. Cost of retirement benefits - non-operating includes amounts related to discontinued product lines and related plant closings totaling \$831,000, \$788,000 and \$812,000 in 2002, 2001 and 2000, respectively. Information regarding the Plan is as follows (in thousands):

	2002 ----	2001 ----
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 9,063	\$ 9,320
Interest cost	611	648
Benefit payments	(953)	(993)
Actuarial (gain) or loss	633	88
	-----	-----
Benefit obligation at end of year	9,354	9,063
	-----	-----
Change in plan assets:		
Fair value of plan assets at beginning of year	3,601	3,914

Edgar Filing: PUBLICARD INC - Form 10-K

Actual return on plan assets	(502)	(407)
Employer contributions	1,064	1,087
Benefit payments	(953)	(993)
	-----	-----
Fair value of plan assets at end of year	3,210	3,601
	-----	-----
Funded status	(6,144)	(5,462)
Unrecognized transition obligation	295	589
Unrecognized net loss	2,306	901
	-----	-----
	\$ (3,543)	\$ (3,972)
	=====	=====

Amounts recognized in statement of financial position consist of:

Accrued benefit liability	\$ (6,144)	\$ (5,462)
Intangible asset	295	589
Accumulated comprehensive loss	2,306	901
	-----	-----
Net amount recognized	\$ (3,543)	\$ (3,972)
	=====	=====

A discount rate of 6.0% and 7.25% was used for December 31, 2002 and 2001, respectively. The expected return on plan assets was 8%.

The components of the net periodic pension cost were as follows (in thousands):

	2002	2001	
	----	----	
Interest cost	\$ 611	\$ 648	\$
Expected return on plan assets	(268)	(317)	
Amortization of transition obligation	293	293	
	-----	-----	-----
Net periodic pension cost	\$ 636	\$ 624	\$
	=====	=====	=====

F-18

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In January 2003, the Company filed a notice with the Pension Benefit Guaranty Corporation ("PBGC") seeking a "distress termination" of the Plan. If the PBGC determines that the Company meets one of the tests for such a termination, the Plan will terminate and the PBGC will become responsible for meeting future retirement obligations of participants (within certain limitations). The Company would be liable to the PBGC for the amount of the unfunded guaranteed benefit obligation. The Company believes that on a termination basis, the Plan's liabilities could exceed the value of its assets by in excess of \$7.0 million. In addition, the Company did not make the required



## Edgar Filing: PUBLICARD INC - Form 10-K

quarterly contribution of approximately \$253,000 that was due on January 15, 2003. The Company has initiated discussions with the PBGC concerning the termination of the Plan and its obligation to the PBGC if the Plan is terminated (including the timing of its repayment obligation). It is not possible to predict the outcome of such discussions.

### NOTE 6 - STOCK OPTIONS AND WARRANTS

The Company has issued stock options pursuant to four fixed stock-based compensation plans, made special stock option awards to certain directors, consultants and employees and also issued common stock purchase warrants in connection with certain subordinated notes. A summary of shares purchasable upon the exercise of stock options and common stock purchase warrants as of December 31, 2002, 2001 and 2000 are as follows:

	2002 ----	2001 ----	2000 ----
Fixed stock-based compensation plans	2,939,175	4,608,450	3,543,750
Special stock options	363,960	535,011	1,824,031
Common stock purchase warrants	--	1,523,573	1,523,573
	-----	-----	-----
	3,303,135	6,667,034	6,891,354
	=====	=====	=====

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 per share. In return, the Company granted a total of approximately 3.1 million replacement stock options on August 20, 2001. The replacement stock options, which were granted under the Company's fixed stock-based compensation plans, generally contain the same terms and conditions of the cancelled stock options and have an exercise price of \$.39 per share, the closing price of the Company's common stock on August 20, 2001.

### FIXED STOCK-BASED COMPENSATION PLANS

The Company has four stock-based compensation plans that provide for the granting of incentive and non-qualified stock options, restricted stock, stock appreciation rights, performance awards and other stock-based awards to employees, non-employee directors and consultants. Under these plans adopted by shareholders of the Company, the Company may grant up to 7,300,000 shares of common stock. The plans are administered by either the Board of Directors of the Company or the Compensation Committee of the Board of Directors. The exercise price of each option granted was equal to the market price of the Company's common stock on the date of grant. Stock options granted to non-employee directors expire five years from the date of grant and vest immediately. Stock options granted to employees generally expire five or ten years from the date of grant. Prior to 1999, stock options granted to employees vested immediately. Grants subsequent to 1998 generally vest over three or four years. As of December 31, 2002, there were 2,244,325 shares available for grant under the fixed stock-based compensation plans.

# Edgar Filing: PUBLICARD INC - Form 10-K

## AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of the stock options issued pursuant to the fixed stock-based compensation plans as of December 31, 2002, 2001 and 2000 and changes during the years then ended is presented below:

	2002		2001		2000	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weight avera exerci pric
Balance at January 1	4,608,450	\$1.07	3,543,750	\$4.63	2,771,167	\$4.1
Granted	90,000	.25	4,171,400	.69	2,322,375	5.3
Exercised	--	--	--	--	(594,167)	1.8
Canceled	(1,759,275)	1.13	(3,106,700)	4.63	(955,625)	6.6
Balance at December 31	<u>2,939,175</u>	1.01	<u>4,608,450</u>	1.07	<u>3,543,750</u>	4.6

A summary of the Company's stock options outstanding and exercisable issued pursuant to the fixed stock-based compensation plans as of December 31, 2002, is as follows:

Range of exercise price	OUTSTANDING			EXERCISABLE	
	Shares	Contractual life	Weighted average exercise price	Shares	Weighted average exercise price
\$ .25-\$ .40	2,358,800	6.7	\$ .38	1,719,267	\$ .38
\$1.37-\$2.72	96,500	1.5	1.82	90,281	1.81
\$2.88-\$3.28	388,375	2.4	3.18	294,375	3.15
\$6.31-\$6.88	95,500	1.6	6.77	93,438	6.81
\$ .25-\$6.88 (all options)	<u>2,939,175</u>	5.8	1.01	<u>2,197,361</u>	1.08

#### SPECIAL STOCK OPTIONS AND STOCK AWARDS

The Company has issued special stock options outside of the fixed stock option plans. As of December 31, 2002, there are a total of 363,960 special stock options outstanding. These options have exercise prices ranging from \$2.00 to \$9.75 per share and all of such options are currently exercisable. In 2000, a total of 583,334 special stock options were exercised with an average exercise price of \$3.22. No options were exercised in 2002 or 2001.

In 2000, pursuant to various employment and separation agreements, the Company issued 50,000 shares of common stock and changed the terms of certain stock options. The fair value of the stock award and the change in terms of the

## Edgar Filing: PUBLICARD INC - Form 10-K

stock options was \$758,000 and was charged to earnings in 2000.

In connection with the Company's business acquisitions in 1998 and 1999, the Company granted options to purchase an aggregate of 1,223,161 shares of common stock to certain employees and owners of the acquired businesses. These options had exercise prices ranging from \$2.00 to \$10.75 per share, generally vest over three years and expire five years from the date of grant. Of these options, 410,000 were granted pursuant to the Company's fixed stock option plans. The fair value of stock options granted amounting to \$5.0 million, was included in the acquisition purchase price. As of December 31, 2002, a total of 203,960 options granted outside of the fixed stock option plans remained outstanding.

In January 1996, the Company issued options to two members of the Company's Board of Directors to purchase 200,000 shares of the Company's common stock at a price of \$2.50 per share for five years. In 2000, a total of 40,000 options were exercised. The expiration date of the remaining 160,000 options was subsequently extended by five years to January 2006.

F-20

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

COMMON STOCK PURCHASE WARRANTS

In December 1986, the Company issued \$30 million of 13% Subordinated Notes together with detachable warrants and underwriter's warrants to purchase a total of 4,800,000 shares of the Company's common stock for five years, which period was subsequently extended by five years. In 1997, the shareholders of the Company approved an additional five-year extension and certain modifications to the warrants. On July 2, 2002, the remaining warrants, entitling the warrant holders to purchase 1,523,573 shares of common stock, expired.

NOTE 7 - COMMITMENTS AND CONTINGENCIES

LEASES

The Company leases certain office space, vehicles and office equipment under operating leases that expire over the next six years. Certain of these operating leases provide the Company with the option, after the initial lease term, to either purchase the property or renew the lease. Total rent expense for all operating leases amounted to approximately \$221,000 in 2002, \$481,000 in 2001 and \$490,000 in 2000.

Minimum payments for operating leases having initial or remaining non-cancelable terms in excess of one year are as follows (in thousands):

YEAR ENDING DECEMBER 31, -----	MINIMUM LEASE PAYMENTS -----	SUBLEASE INCOME -----	NET ----
2003	\$422	\$205	\$217
2004	210	67	143
2005	64	--	64
2006	55	--	55
2007	55	--	55

## Edgar Filing: PUBLICARD INC - Form 10-K

Remainder	40	--	40
	----	----	----
Total minimum lease payments	\$846	\$272	\$574
	=====	=====	=====

The Company and Balfour Investors Inc. ("Balfour") are parties to an agreement, dated as of October 26, 1994, with respect to a portion of the office space leased by the Company in New York City. The Chairman and Vice Chairman of the Company's Board of Directors are the only shareholders of Balfour. The term of the agreement commenced on January 1, 1995 and will expire on June 30, 2004, unless sooner terminated pursuant to law or the terms of the agreement. The agreement provides for Balfour to pay to the Company a portion of the rent paid by the Company under its lease, including base rent, electricity, water, real estate tax escalations and operation and maintenance escalations. Effective March 1, 2002, Balfour's share of rent and other costs was 50% of the total costs incurred. The base rent payable by Balfour under the agreement is approximately \$11,000 per month.

### ENVIRONMENTAL

In April 1996, a consent decree (the "Consent Decree") among the Company, the United States Environmental Protection Agency ("EPA") 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 in Philadelphia previously owned and operated by the Company. Pursuant to the Consent Decree, the Company was obligated to pay a total of \$14.4 million plus interest to the United States and the Commonwealth of Pennsylvania. In January 2002, the Company and the EPA reached an agreement to extend the due date on the remaining unpaid balance through April 2004. In return, the EPA was granted a security interest in certain assets held in escrow.

As discussed in Note 9, in September 2002, the Company reached an agreement pursuant to which the Greenwald Escrow was terminated and net proceeds of approximately \$1.3 million were disbursed to the

F-21

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Company. Upon termination of the Greenwald Escrow in October 2002, the Company satisfied the remaining obligation to the EPA amounting to \$806,000, which included accrued interest.

### GRANTS AND BANK FINANCING

The Company has received grants from several government agencies in the United Kingdom. These grants have been used for marketing, research and development and other governmental business incentives such as general employment. Such grants require the Company to maintain certain levels of operations and employment in Northern Ireland. As of December 31, 2002, the Company has a contingent liability to repay, in whole or part, grants received of approximately \$620,000 in the event the Company becomes insolvent or otherwise violates the terms of such grants.

Infineer has an overdraft facility with a bank in Northern Ireland, which

## Edgar Filing: PUBLICARD INC - Form 10-K

allows for the maximum borrowing of 130,000 British pounds. This facility is secured by all of Infineer's assets and bears an interest rate at the bank's base rate plus 2% (approximately 6% at December 31, 2002). As of December 31, 2002, Infineer had borrowings outstanding under this facility totaling 86,000 British pounds (or the equivalent of \$138,000).

### LEGAL

On May 28, 2002, a lawsuit was filed against the Company in the Superior Court of the State of California, in the County of Los Angeles by Leonard M. Ross and affiliated entities alleging, among other things, misrepresentation and securities fraud. The lawsuit names the Company and four of its current and former executive officers and directors as the defendants. The plaintiffs seek monetary and punitive damages for alleged actions made by the defendants in order to induce the plaintiff to purchase, hold or refrain from selling PublicARD common stock. The plaintiffs allege that the defendants made a series of material misrepresentations, misleading statements, omissions and concealments, specifically and directly to the plaintiffs concerning the nature, existence and status of contracts with certain purchasers, the nature and existence of investments in the Company by third parties, the nature and existence of business relationships and investments by the Company.

Notice of the commencement of this action has been given to the Company's directors and officers liability insurance carriers. The Company believes it has meritorious defenses to the allegations and intends to defend vigorously. In November 2002, the Company and the individual defendants served with the action filed a demurrer seeking the dismissal of six of the plaintiffs' nine purported causes of action. In January 2003, the court ruled in favor of the demurrer and dismissed the entire complaint. The plaintiffs were granted the right to replead and subsequently filed an amended complaint in February 2003. The Company and individual defendants filed a second demurrer in March 2003. The lawsuit is in the early stages. There has been no discovery and no trial date has been set. Consequently, at this time it is not reasonably possible to estimate the damage, or range of damages, if any, that the Company might incur in connection with this action. However, if the outcome of this lawsuit is unfavorable to the Company, it could have a material adverse effect on the Company's operations, cash flow and financial position. Through December 31, 2002, the Company has incurred approximately \$200,000 in defense costs.

Various legal proceedings are pending against the Company. The Company considers all such proceedings to be ordinary litigation incident to the character of its businesses. 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.

### CHANGE OF CONTROL AGREEMENTS

The Company is a party to change of control agreements, which provide for payments to certain 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

F-22

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## Edgar Filing: PUBLICARD INC - Form 10-K

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 of \$842,000 each would be made to the Company's Chairman and Vice Chairman. 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 income taxes on such additional payment, equal to the initial payment before such additional payment and the Company would not be able to deduct these initial or additional payments for income tax purposes.

### INSURANCE RECOVERIES

In February and March 2003, the Company entered into two binding settlements with various historical insurers that would resolve certain claims (including certain future claims) under policies of insurance issued to the Company by those insurers. As a result of the settlements, after allowance for associated expenses and offsetting adjustments, the Company received net proceeds of approximately \$1.0 million in February 2003 and expects to receive an additional estimated \$650,000 in April 2003. Accordingly, the Company expects to recognize a non-recurring gain of approximately \$1.7 million in the first quarter of 2003.

The Company is also in discussions with other insurance markets regarding the status of certain policies of insurance. It cannot be determined whether any additional amounts may be recovered from these other insurers nor can the timing of any such additional recoveries be determined.

### NOTE 8 - SEGMENT DATA

As a result of the disposition of certain operations (See Note 9) and because the Company operates in one industry, that being the deployment of smart card solutions for educational and corporate sites, the Company reports as a single segment. Sales by geographical areas for the years ended December 31, 2002, 2001 and 2000 are as follows (in thousands):

	2002	2001	2000
	----	----	----
United States	\$1,029	\$1,727	\$1,160
Europe	3,445	3,671	4,029
Rest of world	131	254	354
	-----	-----	-----
	\$4,605	\$5,652	\$5,543
	=====	=====	=====

The Company has operations in the United States and United Kingdom. Identifiable assets by country as of December 31, 2002 and 2001 are as follows (in thousands):

## Edgar Filing: PUBLICARD INC - Form 10-K

	2002 ----	2001 ----
United States	\$ 4,842	\$12,037
United Kingdom	2,235	2,557
	-----	-----
	\$ 7,077	\$14,594
	=====	=====

F-23

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9 - DISCONTINUED OPERATIONS

In March 2000, the Company's Board 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 designed, manufactured and distributed 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. In the third quarter of 2000, the Company recognized a gain of \$4.3 million principally related to the sale of Greenwald and Greenwald Intellicard.

In the second quarter of 2001, the Company revised its estimates of proceeds and expenses associated with the wind-down of Amazing and Greystone, which has been substantially completed, and recognized a gain of \$2.4 million, which had been previously deferred pending resolution of certain contingencies. 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.

On September 30, 2002, the Company reached an agreement ("Escrow Termination Agreement") pursuant to which the Greenwald Escrow was terminated and net proceeds of approximately \$1.3 million were disbursed to the Company. Pursuant to the Escrow Termination Agreement, Eastern acknowledged that there were no indemnification claims outstanding under the applicable asset purchase agreement. A gain of \$1.1 million was recognized in the third quarter of 2002, principally relating to the release of reserves upon the resolution of the Greenwald Escrow. 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

## Edgar Filing: PUBLICARD INC - Form 10-K

have been reflected as discontinued operations.

### NOTE 10 - REPOSITIONING CHARGE

As discussed in Note 1, in July 2001, after evaluating the timing of potential future revenues, PublicARD's Board decided to shift the Company's strategic focus. The Company recorded a charge aggregating \$7.3 million in the second and third quarters of 2001 associated with the departure from the smart card reader and chip business. The charge consisted of write-offs of goodwill and intangibles of \$4.1 million and fixed assets of \$554,000, an inventory realizability adjustment of \$1.7 million (included in cost of sales) as a result of the business closure, and severance and other costs of \$1.0 million principally related to the termination of 36 employees. The repositioning activities were substantially completed by December 31, 2001.

F-24

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 11 - SUPPLEMENTAL INFORMATION

Changes in assets and liabilities reflected in the Consolidated Statements of Cash Flows are net of acquisitions of businesses and consisted of the following for the years ended December 31, 2002, 2001 and 2000 (in thousands):

	2002	2001	2000
	----	----	----
Trade receivables	\$ 686	\$ 122	\$ 88
Inventories	(248)	(830)	(714)
Prepaid insurance and other current assets	404	(450)	152
Other assets	533	340	(374)
Net assets of discontinued operations	(404)	(424)	(3,260)
Trade accounts payable	(27)	15	(1,333)
Accrued liabilities	(135)	(2,227)	(607)
Other non-current liabilities	(1,849)	(1,580)	(300)
	-----	-----	-----
	\$ (1,040)	\$ (5,034)	\$ (6,348)
	=====	=====	=====

Cash paid for interest during 2002, 2001, and 2000 was \$81,000, \$79,000, and \$137,000, respectively. No income taxes were paid in 2002, 2001 and 2000. Non-cash investing activities include the acquisition of 35% of Greenwald Intellicard for shares of common stock of \$696,000 in 2000.

Other assets as of December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----



Edgar Filing: PUBLICARD INC - Form 10-K

Investment in minority owned affiliates	\$3,000	\$5,307
Intangible pension asset	295	589
Net assets of discontinued operations	--	886
	-----	-----
	\$3,295	\$6,782
	=====	=====

Accrued liabilities as of December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----
Pension liability	\$1,505	\$1,586
Payroll and other employee benefits	292	409
Environmental obligation	--	434
Deferred revenue	402	166
Other	483	784
	-----	-----
	\$2,682	\$3,379
	=====	=====

Other non-current liabilities as of December 31, 2002 and 2001 consisted of the following (in thousands):

	2002	2001
	----	----
Pension liability and other retiree benefits	\$4,872	\$4,448
Environmental obligation	--	783
Other	118	97
	-----	-----
	\$4,990	\$5,328
	=====	=====

F-25

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The components of other comprehensive loss as of December 31, 2002 and 2001 consisted of the following (in thousands):

2002	2001
----	----

Edgar Filing: PUBLICARD INC - Form 10-K

Foreign currency translation adjustment	\$ 85	\$ 197
Minimum pension liability	2,306	901
	-----	-----
	\$2,391	\$1,098
	=====	=====

Comprehensive loss for the Company includes foreign currency translation adjustments and minimum pension liability, as well as net loss reported in the Company's Statements of Operations. Comprehensive loss for years ended December 31, 2002, 2001 and 2000 was as follows (in thousands):

	2002	2001	2000
	----	----	----
Net loss	\$ (7,193)	\$ (14,821)	\$ (15,400)
Minimum pension liability	(1,405)	(901)	--
Foreign currency translation adjustments	112	(197)	--
	-----	-----	-----
Comprehensive loss	\$ (8,486)	\$ (15,919)	\$ (15,400)
	=====	=====	=====

NOTE 12 - SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The unaudited consolidated financial statements for each of the quarterly periods in the years ended December 31, 2002 and 2001 are as follows (in thousands):

	MAR. 31	JUN. 30	SEP. 30	DEC. 31
	-----	-----	-----	-----
2002				
Net sales	\$ 1,199	\$ 1,016	\$ 1,298	\$ 1,092
Gross margin	563	496	650	441
Loss from continuing operations	(1,269)	(1,227)	(3,409)	(2,354)
Income from discontinued operations	--	--	1,066	--
Net loss	(1,269)	(1,227)	(2,343)	(2,354)
Basic and diluted earnings (loss) per share				
Continuing operations	\$ (.05)	\$ (.05)	\$ (.14)	\$ (.10)
Discontinued operations	--	--	.04	--
	-----	-----	-----	-----
	\$ (.05)	\$ (.05)	\$ (.10)	\$ (.10)
	=====	=====	=====	=====
2001				
Net sales	\$ 1,520	\$ 1,339	\$ 1,575	\$ 1,218
Gross margin	688	(635)	506	557
Loss from continuing operations	(3,509)	(9,510)	(2,799)	(1,353)
Income from discontinued operations	--	2,350	--	--
Net Loss	(3,509)	(7,160)	(2,799)	(1,353)
Basic and diluted earnings (loss) per share				
Continuing operations	\$ (.14)	\$ (.40)	\$ (.12)	\$ (.06)

Edgar Filing: PUBLICARD INC - Form 10-K

Discontinued operations	--	.10	--	--
	-----	-----	-----	-----
	\$ (.14)	\$ (.30)	\$ (.12)	\$ (.06)
	=====	=====	=====	=====

F-26

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

INDEPENDENT AUDITORS' REPORT ON SCHEDULE II

To the Board of Directors and Shareholders of  
PubliCARD, Inc.  
New York, New York

We have audited the consolidated financial statements of PubliCARD, Inc. and subsidiary companies (the "Company") as of and for the year ended December 31, 2002, and have issued our report thereon dated March 24, 2003 (which report expresses an unqualified opinion and includes explanatory paragraphs relating to the Company's ability to continue as a going concern and the application of procedures performed in regards to certain disclosures in the 2001 and 2000 financial statements that were audited by other auditors who have ceased operations and for which we have expressed no opinion or other form of assurance other than with respect to such disclosures). Our audit also included the consolidated financial statement schedule of the Company as of and for the year ended December 31, 2002 listed in Item 15. This consolidated financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audit. In our opinion, such consolidated financial statement schedule, when considered in relation to the basic 2002 consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein. The consolidated financial statements and consolidated financial statement schedules of the Company as of December 31, 2001 and for the years ended December 31, 2000 and 2001 were audited by other auditors who have ceased operations. Those other auditors expressed an unqualified opinion on those consolidated financial statements and consolidated financial statement schedule in their report dated March 20, 2002.

/s/ DELOITTE & TOUCHE LLP

New York, New York  
March 24, 2003

F-27

PUBLICARD, INC.  
AND SUBSIDIARY COMPANIES

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON SCHEDULE

PubliCARD, Inc. dismissed Arthur Andersen LLP on June 5, 2002, and subsequently engaged Deloitte & Touche LLP as its independent auditors. The predecessor auditors' report appearing below is a copy of Arthur Andersen LLP's previously issued opinion dated March 20, 2002. Since PubliCARD, Inc. is unable to obtain a manually signed audit report, a copy of Arthur Andersen LLP's most recently signed and dated report has been included below to satisfy filing requirements, as permitted under Rule 2-02(e) of Regulation S-X.

## Edgar Filing: PUBLICARD INC - Form 10-K

To the Shareholders of PubliCARD, Inc.:

We have audited in accordance with generally accepted auditing standards, the consolidated financial statements of PubliCARD, Inc. and subsidiary companies included in this Form 10-K and have issued our report thereon dated March 20, 2002. Our audits were made for the purpose of forming an opinion on those statements taken as a whole. The schedule listed in the index to consolidated financial statements and schedule is the responsibility of the Company's management and is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic consolidated financial statements. This schedule has been subjected to the auditing procedures applied in the audits of basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

The aforementioned financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has incurred operating losses and requires additional capital to meet its obligations and accomplish the Company's business plan, which raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Arthur Andersen LLP

Stamford, Connecticut  
March 20, 2002

F-28

### PUBLICARD, INC. AND SUBSIDIARY COMPANIES

#### SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 AND 2000

	Balance January 1	Additions		
	-----	Charged to Costs and Expenses	Other (1)	Deductions (2)
	-----	-----	-----	-----
	(in thousand of dollars)			
Year ended December 31, 2002:				
Allowance for doubtful accounts	216	-	-	(113)
Reserve for discontinued operations	1,245	(457)	-	(359)
Year ended December 31, 2001:				
Allowance for doubtful accounts	89	31	158	(62)
Reserve for discontinued operations	3,913	(2,350)	-	(318)
Year ended December 31, 2000:				
Allowance for doubtful accounts	92	28	12	(43)

Edgar Filing: PUBLICARD INC - Form 10-K

Reserve for discontinued operations	4,141	(4,275)	-	4,047
-------------------------------------	-------	---------	---	-------

(1) Other changes for the allowance for doubtful accounts represents reclassifications of previous year receivable reserves included in other operating accounts.

(2) Deductions for allowance for doubtful accounts represent the write-offs of account receivable. Deductions for discontinued operations represent charges and payments to reserves net of gains and receipts credited to reserves.

F-29