Due Diligence Answers –TSI Tailored Systems Inc.

1. A list of all customers by product by revenue starting with largest revenue customer first for the years 2004-2009 & Ytd. 2010
   List is attached. NOTE: These numbers were generated by TSI's billing/accounts receivable system. They are on a calendar-year basis and include deposits. The numbers for Dick's include Golf Galaxy. The numbers for Neiman Marcus include Bergdorf Goodman. The numbers for Stage Stores include Peebles, which Stage purchased in 2004. The numbers for Lord & Taylor include Fortunoff.

2. Full & complete Tax returns for the years 2006-2009
   Sent by Fed Ex. NOTE: These are on a fiscal-year basis. The first year included is from December 2005 through November 2006 and is labeled "2005." The reports are on a cash basis.

3. Complete financial statements for the years 2006-2009
   Sent by Fed Ex. NOTE: These are on a fiscal-year cash basis.

4. W-2 statements for all employees of TSI for the years 2006-2009
   Sent by Fed Ex.

5. List Potential New Work or Projects for remaining 2010 that are not billed
   List is attached.

6. What does it cost a retailer to purchase AdDept software for their advertising Dept? How much does it cost for AxN?
   Because each AdDept installation is so different from the others, there has never been a fixed pricing policy. After the determination of which modules will be included in the first phase of the installation, each new customer is provided with a proposal that can run to ten or so pages. How much we would charge would be based upon the size of the installation in terms of numbers of users and how much software would be used. The minimum charge would likely be around $50,000. In addition, we charge for training at the rate of $1,000 per day plus expenses and custom software, which is detailed in a design document. The latter can easily cost more than the base system.

   The pricing for AxN is currently based on the newspaper's published column-inch rate for ROP. We justify this by saying that the charge is based upon the value of the advertising. The minimum is $25 per month. The maximum is $150. We adjust this for special circumstances. In quite a few cases a number of papers are managed by the same person. We come up with a blended rate that is less than the sum of the individual rates. We charge a few papers extra for the special feature of downloading orders to Excel or a database.

   We also charge the advertisers a modest monthly charge for use of AxN. The primary purpose of this is so that we can truthfully tell the newspapers that the cost

is shared between the advertisers and the newspapers because both benefit from the automated process.

7. How do you price your 2 products? Per user? Per account? Or is it a flat fee for unlimited usage?
We have always charged a flat fee for unlimited usage, but we are open to the idea of a different method of billing. It has to be something that the customer can easily budget and that we can easily manage.

8. How do you bill your customers? Yearly, quarterly, Monthly
Most of the AdDept maintenance agreements are billed monthly. Most of the AxN agreements are billed quarterly. When customers ask for billings on a different cycle, we always comply with the request.

9. How do you determine monthly maintenance fees to your customers?
There is no set formula. It depends primarily on the size of the installation, the modules that are being used, and the difficulty of supporting the account. We charge Dick's extra, for example, because the rules established by the IT department make it so difficult for us to support the account and install changes. We increase the amount of the maintenance on an annual basis. We also increase it when new modules or complex custom programming requests are installed.

10. Do you have contracts with all your customers? If so for how long?
Yes. The contracts do not have an expiration date. Customers must give us thirty days notice if they no longer wish to use AxN or if they no longer want support for AdDept. Only one very small AdDept customer does not have a maintenance contract.

11. Is the AdDept program set up to roll out to other large retail customers? Or do you have to customize each customer's installation?
We have never installed AdDept without some custom programming. It should be noted, however, that all AdDept installations contain all programs, including software designed for other users. Which ones are used at each site is determined by switch settings in the specs file that comes with the installation. Almost all of these settings can only be modified by TSI.

12. Once you add a new customer for the AdDept program, how much labor/technical time does it take to complete the installation of training customer and holding hands thru the learning curve?
The answer to this question varies wildly from one installation to another. We usually tell someone who is planning to use the scheduling and accounting modules to expect to need ten days of on-site training and consulting. This is Mike's time, and it is therefore a burden on him, not the programmers. The first phase could stretch out over months, and more than the projected ten days could be necessary. The end goal is often, but not always, to use AdDept for closing the month. This requires that all of the numbers in AdDept be in precise agreement with the official

numbers at the end of the <u>previous</u> month. This process often unearths problems that never surfaced during the pre-installation period. Sometimes the solution is somewhat time-consuming, and the final reconciliation must be delayed. The problem might well be that the data used to produce the official numbers was incorrectly analyzed, in which case item-by-item reconciliation between AdDept and the official numbers might not be feasible.

Another factor is the amount of cooperation among the users and the strength of the project manager at the client's site. In a few cases an employee critical to the installation has been uncooperative and has slowed down the process.

13. With Mike and 2 programmers how many NEW customers/installations could we add per year for AdDept? AxN?
AxN is unlimited. The support required for each one is minimal.

In the 90's we were doing two or three AdDept installations per year. The staff was slightly larger, but probably not as strong as the current staff. The primary limiting factor is how much new programming is required for each installation.

There is another potential limiting factor that was not present in the 90's. Some of our customers place AdDept inside the wall of systems that are compliant with the Sarbanes-Oxley law. If they do, the difficulty of installing and supporting new code can dramatically increase.

14. How do you measure productivity output of coders/programmers? Per character, per line of code, per project?
We do not use any specific metrics to measure the productivity of programmers. We have a good idea how long we think each portion of each project should take, and we measure the delivery against that standard. However, sometimes difficulties occur for which the programmer should not be blamed. For example, the specs may be faulty or ambiguous, or the programmer may be required to use a technique that is new to him/her. Finally, it should be emphasized that the quality of the work is more important than the speed. There are only two grades in programming: C and F. If the program does what the client wants, you get a C. If not, you get an F.

Since we have never employed dozens of programmers, we have never seen the need to use a formal process to evaluate productivity. Because we work so closely with them, we have always had a good feel about each individual's productivity.

15. How do you safeguard and protect the source code from employees if they decide to leave and compete against you?
This has never been an issue or even a potential issue. In the first place, no other company that we have ever heard of has marketed anything remotely comparable to AdDept in the last decade, so there is no one to hire employees away. They would have to start the business or at least the line of business themselves. The programmers who have worked for us have had neither the ability nor the inclination

to attempt this. Furthermore, although the programmers know fairly well how individual programs work, even ones who have worked at TSI for years have only a sketchy idea of how the intricacies of retail advertising and especially the accounting work. The most valuable AdDept programs are also the most complicated ones, and they would be difficult in the extreme to replicate or even support.

A programmer who did manage to obtain the source code would be faced with several exceedingly difficult technical problems. A large investment in infrastructure would be required in order to mimic the one used by TSI. For technical reasons this would be much more difficult than it sounds. Some of the methods that we use are by no means off-the-shelf. In fact, one of the most important compilers would be impossible for practically anyone to obtain.

The worst difficulty for an upstart would be trying to market the system. No one besides Mike has ever done a demo of any of these systems, and no one else has put together a proposal and a design document. At this point in time it is almost impossible to imagine any potential user willing to pay to be the first guinea pig for someone else.

16. How do you calculate and cost out time and labor for new projects? ie..new sales use tax project
We make a rough estimate of the number of hours or days that we expect the project to take and add a small cushion. This is the <u>minimum</u> that we would charge. The amount that we would actually quote would be based on what we think that the client would be willing to pay based upon the perceived value of the product. If we think that it might be marketable to other clients, we might also take that into account.

17. When was your last price increase for both products? How much was it?
We do not have a fixed price for the AdDept product. We increased our maintenance by 5 percent last year. We have never really increased our prices for AxN. If anything, the column-inch rates have been decreasing with the decrease in circulation for most newspapers.

18. How many NEW customers have you added in the last 4 years?
Our last two new AdDept installations were at Marshall Field's (now Macy's) in 2005 and Macy's South in 2006. We did an installation for Golf Galaxy on Dick's computer and for Fortunoff (now defunct) on the Lord & Taylor box in late 2008. In 2009 we enhanced the installation on the Neiman Marcus system to include Bergdorf Goodman and Neiman's catalog business.

From 2002 through 2008 the number of AxN installations increased every year as a result of the expansion of Belk and especially Dick's. This has been reversed in the last year because of the consolidation of all of Macy's advertising functions in New York. The New York division has never used AxN.

19. How many customers have you lost in the last 4 years?
No retailers have dropped AdDept, but several AdDept installations have disappeared in the last few years because of the consolidation of department store divisions and the merger of our two largest clients, Macy's and the May Company.

20. What are the top 5 most compelling reasons a new customer would purchase the AdDept program?
1. AdDept has the potential to address whatever problems the retailer has been unable to handle with its current approach. It is difficult to tell ahead of time which problem has been given short shrift before the completion of the on-site evaluation. This is not a cop-out. We are often surprised that what seems like a simple problem to us is beyond the means of approaches used by prospective clients.

2. AdDept provides one version of the truth. It eliminates the situation in which everything looks good using one person's data but bad with another's. If anyone disputes AdDept's numbers, audit trails are in abundance.

3. AdDept provides the tools for accurate and verifiable allocation of expenses to stores and/or merchandise groups.

4. AdDept allows the advertising department to adapt to changing internal and external conditions without worrying about the length of the IT department's project list. This should perhaps be number one on the list, but it is difficult for some prospective users to envision what a valuable partner TSI will be to them as they adjust to changing market conditions. In fact, it is when dramatic changes occur that we often see a surge in our business. The impetus for the Belk installation, for example, occurred when Belk consolidate the administration of its four divisions in Charlotte, NC.

5. AdDept facilitates the collection of co-op. In several cases this has more than justified the cost of the system in the first year of operation.

AxN program?
1. No missed ads means no make-goods.

2. The advertiser wants them to use it. If the advertiser makes this very clear, the newspaper will almost certainly agree.

3. The system is convenient and easy to use.

4. The history of each order is available. No one ever disputes the existence or the specifics of any order.

5. The printouts of the web pages are very easy to read.

21. How do retail Advertising departments manage all their information if they are NOT using AdDept? What are they doing without it?
A few may have developed something on their own. One of our customers told us years ago that Dillard's had a mainframe system that its advertising departments used. Most of the other big retailers have developed elaborate spreadsheets or databases (like Access or Filemaker Pro) that may or may not be connected. They may have a module from their ERP system that they have bent around to use for advertising. Before implementing AdDept, for example, Belk employed two general ledger systems, one for advertising and one for accounting. This may be the most outstanding example of the old saying: "If your only tool is a hammer, all your problems look like nails." Some retailers may have purchased a software system to help with scheduling in some media. There are quite a few packages for broadcast and a couple for newspaper. They generally emphasize managing the buys, not managing expenses.   There are work-flow systems for the creative and production areas.

22. What is the process to close a deal with a large retail customer who is considering purchasing AdDept….how quickly or slowly does it happen?
1. Schedule a visit for the purpose of fact collection. The customer may not want this step, but without the knowledge gained in this process the sale is much more difficult. At this time samples of every piece of output that they use in the areas being covered is collected and analyzed.

2. Try to get IT on board. It is absolutely critical to determine IT's parameters for approving a project like this.

3. Give a demo. The emphasis is that AdDept provides a flexible structure around which concrete solutions for the department's specific problems will be constructed.

4. Provide a detailed written proposal with a design document that outlines everything that we plan to provide with custom programming. This often includes projected time lines, too.

5. Wait for approval. Sometimes they need to get capital, and that requires political connections. It could take several months.

There may be a better process that this, but this one has worked for us.

23. What would the objections be from a large retail customer of why they would NOT want AdDept. for their business?
The most likely objection is that they were unable to get capital for the project. In the last couple of years capital has been extremely scarce.

The second most likely objection is that the IT department objects to something about TSI's approach. For example, they may be unfamiliar with the hardware and

not want to support it. Another possible problem is that someone's career in the IT department depends upon the continuation of the company's current approach.

If the decision-maker is accustomed to using web-based or graphical system, he/she may object to AdDept's text-based front end.

In previous years the worry that a company of our size might not be around to support the system was prevalent, but history has proven that this reasoning is definitely flawed.

24. What NEW markets could AdDept be adapted for?
Any retailer that does a lot of advertising could profitably use AdDept. The approach used by Dick's, for example, would be appropriate for any of the home improvement, drugs, office supplies, sporting goods, electronics, and discount department store chains. There may well be others.

We have heard that advertising by retailers in other countries is similar to that of advertising in the United States, but we have never researched this idea.

It is possible that in-house advertising departments that are not retailers could have use for some sections of AdDept. However, many of the most involved accounting programs would not be appropriate for them.

If an AdDept installation could be hosted on a system run by TSI or some other company, the involvement of the IT people would be much more limited, and the capital investment and Sabanes-Oxley problems could conceivably be eliminated. That could potentially make AdDept an attractive alternative for a much larger set of users.

AxN the butterfly system?
With the current business model, the AxN income is dependent upon AdDept installations, but that is not the only conceivable business model. For example, if we could get the Newspaper Association of America to sponsor AxN as a standard for its members, we could stop billing individual newspapers and start billing the advertisers. We could then set up interfaces with various software packages used by ad agencies to schedule newspaper space. This could be done by constructing a standard interface using XML or something similar or by negotiating with the ad agency vendors one at a time.

We could approach retailers not using AdDept to gauge their interest in using AxN. This would require a good bit of custom programming to take whatever files that their systems, if any, can provide and put them in a format that AxN could process. We could also approach advertising agencies that specialize in newspaper or ones that represent customers who buy a lot of newspaper space (AT&T, Verizon, Sprint, etc.). The custom programming issue would be similar.

The butterfly approach could be applied to any other area in which one customer places essentially the same order with a lot of different businesses and does this repeatedly. We have been involved with advertising for such a long time that it is hard for us to think of many of these outside of the media area.

25. Realistically how many new customers could we add each year for AxN?
No limit. The computer does most of the work, and it is nowhere near its capacity.

AdDept?
We could handle at most two or three installations per year that require a considerable amount of custom programming.

26. Have you ever hired any sales person to sell for TSI? If so, how did they do?
We had a full-time sales person in the late nineties. It took him quite a bit of time to get started (his experience was in retail advertising, not sales), but once he got going he generated as much work as we could possibly handle.

27. Do you have any Trademarks?
No.

Copywrites?
No.

Patents?
No.

Web URL's you own?
TSItailoredsystemsinc.com, tsi-tsi.com, and tsi-tsi2.com.

28. What type of employment agreements do you have with your coders/programmers?(please include a copy)
None.

29. What NEW projects are in house for 2010? What kind of revenue will they generate?
Approximately twenty projects worth about $110,000 have been approved but not yet delivered. About forty additional projects worth about $160,000 have been quoted. Some portion of the latter will be approved, but it is difficult to say how much.

30. Who is your competition for AxN?
One ad agency that we know of uses its own website for insertion orders. We do not consider them competition because the only company that uses it, to our knowledge, is the agency itself. So, an advertiser that wanted to use it would have to hire the agency to place its ads, not just to manage the orders. No one else that we know of has attempted to get the newspapers to subscribe to a service.

One of our customers hired someone to create an e-mail-based insertion order system for them. They considered using AxN, but, because they use a very large number of very small papers, they were worried that a high percentage of them would not subscribe. They did not want to run two insertion order systems, one for subscribers and something else for non-subscribers.

AdDept?

To our knowledge there is no system that is even roughly comparable to AdDept. A few systems address some areas that AdDept covers, especially media scheduling and trafficking of production of ads.

31. What Language is the software developed in?

AdDept is written in BASIC, RPG, CL, and SQL. The client end of AxN is written in Net.Data and JavaScript. We have explored the possibility of converting the Net.Data part to PHP. The server end is in BASIC, CL, and SQL.

32. Is there a large skill pool of programmers/coders to pull from as we grow the business?

No. We expect to need to provide a lot of training to any new programmer. Teaching them all of the programming languages and the structured programming techniques that we use is the least of it. Learning how retail advertising works is much more difficult. Prospective hires have generally learned the techniques for picking up new programming languages in school or work. There are no classes in retail advertising.

33. How do your customers interface their systems with AdDept?

Most of our customers have interfaces between AdDept and their accounting systems in some or all of the following areas: expense invoices, co-op billing, journal entries for media accruals, journal entries for non-media accruals, journal entries for co-op accruals, journal entries for prepaid to expense, journal entries for use tax. Some of our customers also upload data into AdDept from broadcast buying systems or from the system that they use to manage the quantities of mailings by store. One customer has an elaborate two-way interface with its co-op contract system. One has a two-way interface with its accounting system.

34. Are TSI interfaces based on industry standards such as Web services or Message based queues?

No. The customer provides us the format of the file required by the accounting system, and we write code that puts the records in these formats. Using the more flexible formats would require that the customer's IT department write and support code to translate the standard format to the one recognized by its accounting system.

Most of our interfaces have been around a lot longer than web services. We have no objection to using new methodologies for new interfaces.

35. Are there imbedded software products that require licensing from 3rd parties?
Absolutely not.

36. Do customers have the ability to access their data in the system if they want to data mine?
Yes. We spend a fair amount of time teaching the advertising people how to do this. Some do it with enthusiasm; others want us to write reports for absolutely everything.

37. On a daily basis on average how much time is spent from the staff on customer support?
This requires some research. We will provide the answer later.

38. How many trouble tickets per month are worked and the average time to closure?
This also requires some research. We use our problem system to track things that would not require trouble tickets in most system. We will provide the answer later.

39. For a newly added customer, what exactly are the costs to deploy and install the AdDept software on the customers hardware?
The only costs to TSI are during the sales cycle. After the contract is signed, everything is billed to the customer.

A. How many trips to customer site to install and train staff
Anywhere from three to ten or more.

B. How much time and expense is associated with getting a new customer up and going on the system?
The customer pays $1,000 per day for training and consulting plus expenses. The customer determines how many days.

40. What Obsolesence factors are involved with AdDept and AxN?
A. Costs?
B. How often is the software revised to avoid obsolescence?
We cannot think of anything like this since the massive Y2K project. If the company that supports the customer's accounting software changed the interface, we might need to do something. If a customer changed accounting packages, we would almost certainly need to do something.

IBM no longer supports Net.Data, which is a scripting language for generating HTML. If significant enhancements to the interface for AxN are envisioned, they should probably be done in PHP rather than Net.Data.

C. Are there 3rd party software modules that if upgraded can affect AdDept?
There was a problem with the broadcast interface with one software product in the early 90's, but nothing since then. One of our customers changed its accounting software, but their IT department wrote a module to convert the file that we provided for the old system.

41. How do customers get the latest updates/upgrades on AdDept? Is it thru a
    1) CD update that they install or thru a Web interface portal that allows updates quickly?
No. We do all installs remotely, usually on weekends. We must take great care to make absolutely sure that everyone's data files and programs are at the same level. This is by far the most efficient way for us to do this. It would be extraordinarily time-consuming to automate the installation of upgrades. It would probably cut our efficiency in half or maybe even more than that.