

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

FINANCIAL REPORT

December 31, 2003

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To the Board of Directors
Sample Government Contractor / Technology, Inc.
Anytown, USA

We have reviewed the accompanying balance sheet of Sample Government Contractor /Technology, Inc. (an S-Corporation) as of December 31, 2003, and the related statements of income, retained earnings and cash flows for the year then ended, in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management of Sample Government Contractor / Technology Inc.

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

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

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

Silver Spring, Maryland
May 3, 2004

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

**BALANCE SHEET
December 31, 2003**

ASSETS

CURRENT ASSETS

| | |
|---------------------------------|------------------|
| Cash | \$ 281,326 |
| Contracts receivable - billed | 884,150 |
| Contracts receivable - unbilled | 225,430 |
| Employee advances | 5,493 |
| Loan receivable, officer | 50,000 |
| Prepaid insurance | 12,382 |
| Prepaid expenses | <u>3,722</u> |
| Total current assets | <u>1,462,503</u> |

PROPERTY AND EQUIPMENT, at cost

| | |
|-------------------------------|----------------|
| Computer equipment | 190,480 |
| Furniture and fixtures | 67,602 |
| Vehicles | 31,413 |
| Computer software | 69,988 |
| Leasehold improvements | <u>79,762</u> |
| | 439,245 |
| Less accumulated depreciation | <u>139,737</u> |
| Total property and equipment | <u>299,508</u> |

OTHER ASSETS

| | |
|-----------------------------|---------------------|
| Deposits | 23,495 |
| Patent, net of amortization | <u>15,463</u> |
| | <u>\$ 1,800,969</u> |

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES

| | |
|--|--------------|
| Accounts payable | \$ 227,450 |
| Accrued wages and payroll taxes | 245,386 |
| Accrued profit sharing contribution | 83,970 |
| Accrued expenses | 43,525 |
| Notes payable, current portion | 161,820 |
| Bank line of credit payable | 43,534 |
| Capital lease payable, current portion | <u>1,491</u> |

Total current liabilities 807,176

LONG-TERM DEBT

| | |
|------------------------------------|----------------|
| Notes payable, non current portion | <u>246,180</u> |
|------------------------------------|----------------|

STOCKHOLDERS' EQUITY

| | |
|---|----------------|
| Common stock, \$1 par value; 1,000 shares authorized, 100 shares issued, and outstanding | 100 |
| Additional paid-in capital | 20,040 |
| Retained earnings | <u>727,473</u> |

Total stockholders' equity 747,613

\$ 1,800,969

SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

STATEMENT OF INCOME
For the Year Ended December 31, 2003

| | |
|---|--------------------------|
| Earned revenue | \$ 9,805,585 |
| Direct costs | |
| Direct labor | 895,268 |
| Other direct charges | <u>5,915,479</u> |
| Total direct costs | <u>6,810,747</u> |
| Gross profit | <u>2,994,838</u> |
| Operating expenses | |
| Fringe benefits | 596,776 |
| Overhead | 518,668 |
| Research and development | 168,988 |
| General and administrative | <u>1,149,099</u> |
| Total operating expenses | <u>2,433,531</u> |
| Operating income | <u>561,307</u> |
| Financial income or expense, net, including interest expense of \$26,185 | <u>(10,681)</u> |
| Net income | <u><u>\$ 550,626</u></u> |

SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

**STATEMENT OF RETAINED EARNINGS
For the Year Ended December 31, 2003**

| | |
|--------------------|--------------------------|
| Balance, beginning | \$ 176,847 |
| Net income | <u>550,626</u> |
| Balance, ending | <u><u>\$ 727,473</u></u> |

SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2003

Cash flows from operating activities:

| | |
|---|-------------------|
| Net income | \$ 550,626 |
| Adjustments to reconcile net income to net cash provided by operations: | |
| Depreciation | 49,604 |
| Amortization | 2,030 |
| (Increase) decrease in: | |
| Contracts receivable - billed | 6,400 |
| Contracts receivable - unbilled | (35,884) |
| Employee advances | (3,989) |
| Loan receivable, officer | (50,000) |
| Prepaid insurance | (1,128) |
| Prepaid expenses | (2,467) |
| Deposits | (18,882) |
| (Decrease) increase in: | |
| Accounts payable | (176,240) |
| Accrued wages and payroll taxes | 32,933 |
| Accrued profit sharing contribution | 11,424 |
| Accrued expenses | (5,037) |
| Net cash provided by operating activities | <u>359,390</u> |
| Cash flows from investing activities: | |
| Purchases of property and equipment | <u>(85,530)</u> |
| Net cash used in investing activities | <u>(85,530)</u> |
| Cash flows from financing activities: | |
| Payment of bank line of credit | (60,617) |
| Principal payments of bank notes | (132,570) |
| Payment of capital lease obligations | <u>(3,468)</u> |
| Net cash used in financing activities | <u>(196,655)</u> |
| Net increase in cash | 77,205 |
| Cash, beginning of year | <u>204,121</u> |
| Cash, end of year | <u>\$ 281,326</u> |

SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2003

Note 1 Summary of significant accounting policies

Description of business

Sample Government Contractor / Technology Inc. (the Company) was incorporated on January 3, 1994 in the State of Maryland. The company provides telecommunication services, including leased telephone lines and administrative support, to U.S. Government agencies and prime contractors thereto, on an unsecured basis. The company maintains one location in Maryland and staff at various Government sites.

The accounting policies relative to the carrying value of property and equipment are indicated in the captions on the balance sheet. Other significant accounting policies are as follows:

Method of accounting

Assets, liabilities, income and expenses are reported using the accrual basis of accounting, whereby income is recorded when sales are made and expenses as incurred.

Depreciation

Depreciation expense is calculated by using accelerated methods based on the estimated useful lives of the assets:

| | |
|------------------------|-----------|
| Computer equipment | 5 years |
| Furniture and fixtures | 5-7 years |
| Vehicles | 5 years |
| Computer software | 3 years |
| Leasehold improvements | 10 years |

Depreciation expense totaled \$49,604 for the year ended December 31, 2003.

Research and development costs

All research and development costs were charged to expense when incurred. Research and development costs were \$168,988 for the year ended December 31, 2003.

Statement of cash flows

The Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2003

Note 1 Summary of significant accounting policies (continued)

Recognition of contract revenue

Contract revenue is derived principally from time and material and fixed-priced, long-term and short-term contracts. Revenue on time and material contracts is recognized based on a fixed hourly rate for direct labor hours expended. The fixed rate includes direct labor, indirect expenses, and profit. Materials and other specified direct costs are reimbursed at actual costs. Revenue on fixed-price contracts is recognized on the percentage-of-completion method of accounting based on costs incurred to date in relation to total estimated costs. Anticipated losses are recognized as soon as they become known.

Leases

Leases that meet certain criteria are classified as capital leases. Assets and liabilities are recorded at amounts equal to the fair value of the leased properties at the beginning of the respective lease terms. These assets are depreciated over their estimated useful lives. Interest expense relating to the lease liabilities is recorded to effect constant rates of interest over the terms of the leases. Leases that do not meet such criteria are classified as operating leases and related rentals are charged to expenses as incurred.

Patents amortization

Patents costs are being amortized on a straight-line basis over seventeen years. Amortization expense amounted to \$2,030 the year ended December 31, 2003.

Income taxes

On January 1, 1997, the Company elected to be treated as an S corporation for Federal and state income tax purposes and, accordingly, elements of income and expense pass through directly to the shareholders.

Use of estimates in preparation of financial statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that effect the amounts reported on the financial statements and accompanying notes. Actual results could differ from those estimates.

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2003

Note 2 Concentration of credit risk

At December 31, 2003 the Company has cash balances of \$181,326 in excess of the \$100,000 Federal Deposit Insurance Corporation limits. The Company does not believe there are significant risks associated with these excess cash balances.

Note 3 Contract receivables

At December 31, 2003, contract receivables consist of the following:

| | |
|---------------------------------------|-------------------|
| Contract revenue billed: | |
| U.S. Government | \$ 539,129 |
| Commercial customers | <u>345,021</u> |
| Contracts receivable | 884,150 |
| Less: allowance for doubtful accounts | <u>- -</u> |
| | <u>\$ 884,150</u> |
| Contract revenue unbilled: | |
| U.S. Government | \$ 134,275 |
| Commercial customers | <u>91,155</u> |
| Contracts receivable | 225,430 |
| Less: allowance for doubtful accounts | <u>- -</u> |
| | <u>\$ 225,430</u> |

The unbilled portion of accounts receivable relates to jobs substantially complete at the end of the fiscal year, but not billed until the beginning of the following year. The Company considers contracts receivable to be fully collectible; accordingly, no allowance for doubtful accounts is required. If amounts become uncollectible, they will be charged to operations when that determination is made.

Note 4 Major customer

Over 51% of the corporation's revenue was from various agencies of the federal government through prime contracts and subcontracts, which operate with the oversight of DCAA, with time and material contracts, cost-plus contracts and cost-plus-fixed-fee contracts.

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2003

Note 5 Related parties

The Company had an outstanding receivable of \$50,000 from one of its principal shareholders, an officer, as of December 31, 2003. No interest was charged on this loan.

Note 6 Bank line of credit payable

The Company has a line of credit in the amount of \$200,000 with U.S. Confidential Bank. Interest is payable monthly at 2% above the prime lending rate. At December 31, 2003, the Company had drawn \$43,534 against this line. The line of credit is secured with a blanket lien on corporate assets and is personally guaranteed by the Company's three principal shareholders.

Note 7 Long term debt

Notes payable at December 31, 2003 consist of the following:

| | |
|---|-------------------|
| Secured equipment installment note, in equal monthly principal installments of \$7,030 plus interest at 6.9% per annum, is due in December 2006 | \$ 253,080 |
| Unsecured note payable, in equal monthly principal installments of \$6,455 each Month plus interest at 7.1% per annum, is due in December 2005 | <u>\$ 154,920</u> |
| Total notes payable | 408,000 |
| Less: current portion | <u>161,820</u> |
| Total long term debt | <u>\$ 246,180</u> |

Aggregate maturities or payments required on principal under long-term debt obligations for each of the succeeding five years are as follows:

| | |
|--------------------------|-------------------|
| Year ending December 31, | |
| 2004 | \$ 161,820 |
| 2005 | 161,820 |
| 2006 | 84,360 |
| 2007 | -- |
| 2008 | <u>--</u> |
| | <u>\$ 408,000</u> |

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Note 8 Operating leases

The Company conducts its operations from a facility that is leased under a five-year non-cancelable operating lease expiring in June of 2007. The terms of the lease include base annual rent with annual operating expense and consumer price index increases. The Company's three principal shareholders personally guarantee this lease. The Company recorded \$95,906 in rental expense for the year ended December 31, 2003.

The following is a schedule of future minimum rental payments required under the above operating lease as of December 31, 2002.

| Year Ending December 31, | |
|--------------------------|-----------|
| 2004 | \$ 98,783 |
| 2005 | 101,747 |
| 2006 | 104,799 |
| 2007 | 107,943 |
| 2008 and beyond | 55,590 |

Note 9 Backlog

Backlog represents the amount of revenue the Company expects to realize from work to be performed on uncompleted contracts, both in progress and not yet started at year-end. The following is a reconciliation of backlog representing signed contracts in existence at December 31, 2003:

| | |
|--|---------------------|
| Backlog balance at December 31, 2002 | \$ 8,794,523 |
| New contracts during the year | 7,764,890 |
| Contract adjustments | <u>559,000</u> |
| | 17,118,413 |
| Less contract revenue earned during the year | <u>9,805,585</u> |
| Backlog balance at December 31, 2003 | <u>\$ 7,312,828</u> |

In addition, the Company signed additional contracts totaling \$3,214,505 between January 1, 2004 and the date of this report.

Note 10 Cash flow statement disclosure

| | |
|--|-----------|
| Cash paid in 2003 for interest expense | \$ 26,185 |
| Cash paid in 2003 for income taxes | -- |

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2003

Note 11 Capital leases

The Company is the lessee of an IBM Big Blue Computer under a capital lease expiring in June 2004. The asset and liability under the capital lease is recorded at the present value of the minimum lease payments. The asset is depreciated over the lease term of 60 months. Depreciation of the asset under the capital lease is included in depreciation expense for 2003.

The following is an analysis of leased property under capital leases at December 31, 2003:

| | |
|-------------------------------|-----------------|
| Computer equipment | \$ 71,673 |
| Less accumulated depreciation | <u>62,980</u> |
| | <u>\$ 8,693</u> |

The following is a schedule by year of future minimum lease payments under capital leases together with the present value of net minimum lease payments as of December 31, 2003:

| | |
|---|--------------|
| Year ending December 31, | |
| 2004 | \$ 1,566 |
| 2005 | -- |
| 2006 | -- |
| 2007 | -- |
| 2008 | <u>--</u> |
| Net minimum lease payments | 1,566 |
| Less amount representing interest | <u>75</u> |
| Present value of net minimum lease payments | 1,491 |
| Less current portion | <u>1,491</u> |
| | <u>\$ --</u> |

Note 12 Retirement plan

The Company has a profit sharing plan. The retirement plan is for all eligible employees with one year of service. Plan entry dates are January 1, and July 1. The profit sharing plan is a discretionary plan in which the Company can contribute up to 15% of the wages of eligible participants. During the year ended December 31, 2003, the Company accrued \$ 83,970 in contributions to this retirement plan.

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Note 13 Stock option plan

The Company has stock option plans for directors, officers, and employees, which provide for nonqualified and incentive stock options. Stock options are granted to employees and directors at an exercise price equal to the fair market value of the company's stock at the date of grant. Generally, options vest 25 percent per year, are fully vested four years from the grant date and have a term of ten years. The following tables summarize option activity under the Plans during 2003, 2002 and 2001:

| | <u>2003</u> | | <u>2002</u> | | <u>2001</u> | |
|--------------------|---------------------------|-------|---------------------------|-------|---------------------------|-------|
| | Weighted-average exercise | | Weighted-average exercise | | Weighted-average exercise | |
| | Shares | price | Shares | price | Shares | price |
| Balance, 1/1 | 2,718 | \$36 | 1,988 | \$35 | 1,548 | \$24 |
| Options granted | 1,650 | 25 | 1,560 | 30 | 1,230 | 45 |
| Options exercised | (640) | 10 | (480) | 12 | (560) | 14 |
| Options expired | <u>(480)</u> | 36 | <u>(350)</u> | 40 | <u>(230)</u> | 24 |
| Balance, 12/31 | <u>3,248</u> | 30 | <u>2,718</u> | 36 | <u>1,988</u> | 35 |
| Exercisable, 12/31 | <u>1,540</u> | \$32 | <u>1,224</u> | \$27 | <u>964</u> | \$20 |

Information about options outstanding was as follows at December 31, 2003:

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Note 13 Stock option plan (continued)

| | Options outstanding | | | Options exercisable | |
|---------------|--|---|---|---------------------|-------|
| | Weighted- average remaining life in Shares | Weighted- average exercise price | Weighted- average exercise price | Shares | price |
| \$0-\$19.99 | 782 | 1.8 | \$12 | 782 | \$12 |
| \$20-\$39.99 | 1,486 | 6.2 | 33 | 424 | 35 |
| \$40 and over | 980 | 7.4 | 54 | 334 | 55 |
| | 3,248 | 6.5 | \$30 | 1,540 | \$32 |

The Company follows Accounting Principles Board Opinion 25, Accounting for Stock Issued to Employees, to account for stock option and employee stock purchase plans. An alternative method of accounting for stock options is SFAS 123, Accounting for Stock-Based Compensation. Employee stock options are valued at grant date using the Black-Scholes valuation model, and this compensation cost is recognized ratably over the vesting period.

SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

**INCOME STATEMENT DETAIL
For the Year Ended December 31, 2003**

OPERATING EXPENSES

FRINGE BENEFITS

| | |
|--------------------------------|------------|
| FICA/Medicare expense | \$ 139,964 |
| Medical and hospital insurance | 131,940 |
| Vacation wages | 108,086 |
| Profit sharing plan | 83,970 |
| Holiday wages | 56,285 |
| Sick leave wages | 22,833 |
| Unemployment insurance | 16,305 |
| Disability insurance | 12,010 |
| Employee morale | 9,190 |
| Life insurance | 7,894 |
| Vision insurance | 4,084 |
| Military leave | 2,459 |
| Severance pay | 1,756 |

SUBTOTAL 596,776

OVERHEAD

| | |
|------------------------------------|---------|
| Overhead salaries | 202,752 |
| Officers' salary | 174,582 |
| Depreciation | 32,860 |
| Telephone expenses | 22,161 |
| Office supplies | 15,483 |
| Property rental | 13,954 |
| Professional fees | 13,386 |
| Training | 8,118 |
| Contracted labor | 7,563 |
| General liability insurance | 5,564 |
| Property insurance | 4,251 |
| Equipment rental | 4,019 |
| Travel and entertainment allowable | 2,832 |
| Utilities | 2,691 |
| Bank service charge | 2,245 |
| Amortization | 1,347 |
| Meals allowable | 1,128 |
| Cleaning expenses | 1,103 |
| Auto expense | 820 |
| Membership dues | 615 |
| Postage and shipping | 568 |
| Equipment repairs and maintenance | 538 |
| Repairs and maintenance | 88 |

SUBTOTAL 518,668

RESEARCH AND DEVELOPMENT

| | |
|-----------------------|---------|
| Professional services | 155,258 |
| Regular salaries | 13,299 |
| Office supplies | 431 |

SUBTOTAL 168,988

SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

**INCOME STATEMENT DETAIL
For the Year Ended December 31, 2003**

GENERAL AND ADMINISTRATIVE

| | |
|-------------------------------------|--------------|
| General and administrative salaries | 344,910 |
| Officers' salary | 302,372 |
| Professional fees | 113,876 |
| Property rental | 82,032 |
| Depreciation | 16,744 |
| Contracted labor | 15,404 |
| Office supplies | 11,325 |
| Telephone expenses | 10,011 |
| Equipment repair and maintenance | 7,005 |
| Property insurance | 5,201 |
| Bank service charges | 4,691 |
| Equipment rental | 4,563 |
| Travel and entertainment allowable | 4,277 |
| Utilities | 3,782 |
| General liability insurance | 3,277 |
| Meals allowable | 2,980 |
| Cleaning expenses | 2,017 |
| Repair and maintenance | 1,452 |
| Training | 994 |
| Amortization | 683 |
| Auto expenses | 463 |
| Postage and shipping | 457 |
| Membership dues | 397 |
| Bid and proposal expenses | |
| Professional fees | 58,339 |
| Regular salaries | 19,973 |
| Travel allowable | 3,140 |
| Rent | 1,474 |
| Telephone | 959 |
| Meals allowable | 800 |
| Auto expense | 339 |
| Office supplies | 241 |
| Marketing expenses | |
| Regular salaries | 67,638 |
| Professional fees | 34,732 |
| Travel allowable | 5,554 |
| Auto expense | 3,275 |
| Meals allowable | 1,371 |
| Office supplies | 1,347 |
| Unallowable costs | |
| Officers' salary | 4,610 |
| Employee morale | 2,485 |
| Travel and entertainment | 1,859 |
| Charitable contribution | 1,086 |
| Meals | 964 |
| SUBTOTAL | 1,149,099 |
| TOTAL OPERATING EXPENSES | \$ 2,433,531 |

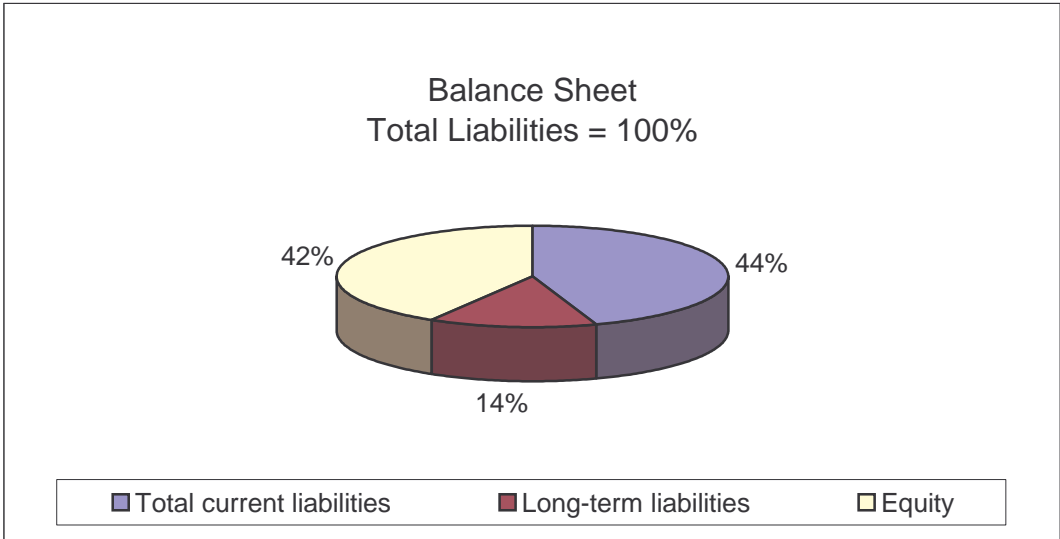
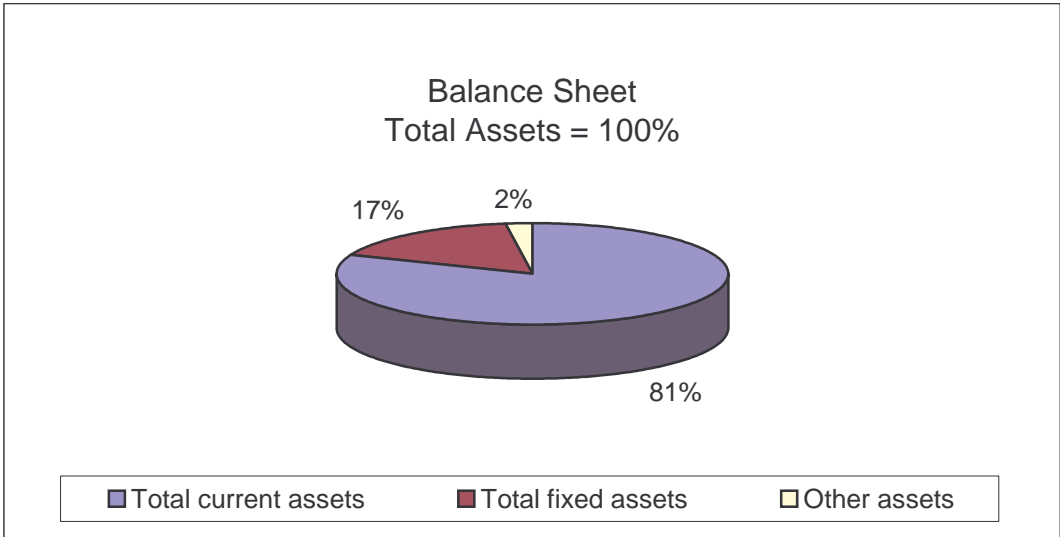
SEE ACCOUNTANTS' REVIEW REPORT

The Notes to Financial Statements are an integral part of this statement

APPENDIX
GRAPHICAL ANALYSIS

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

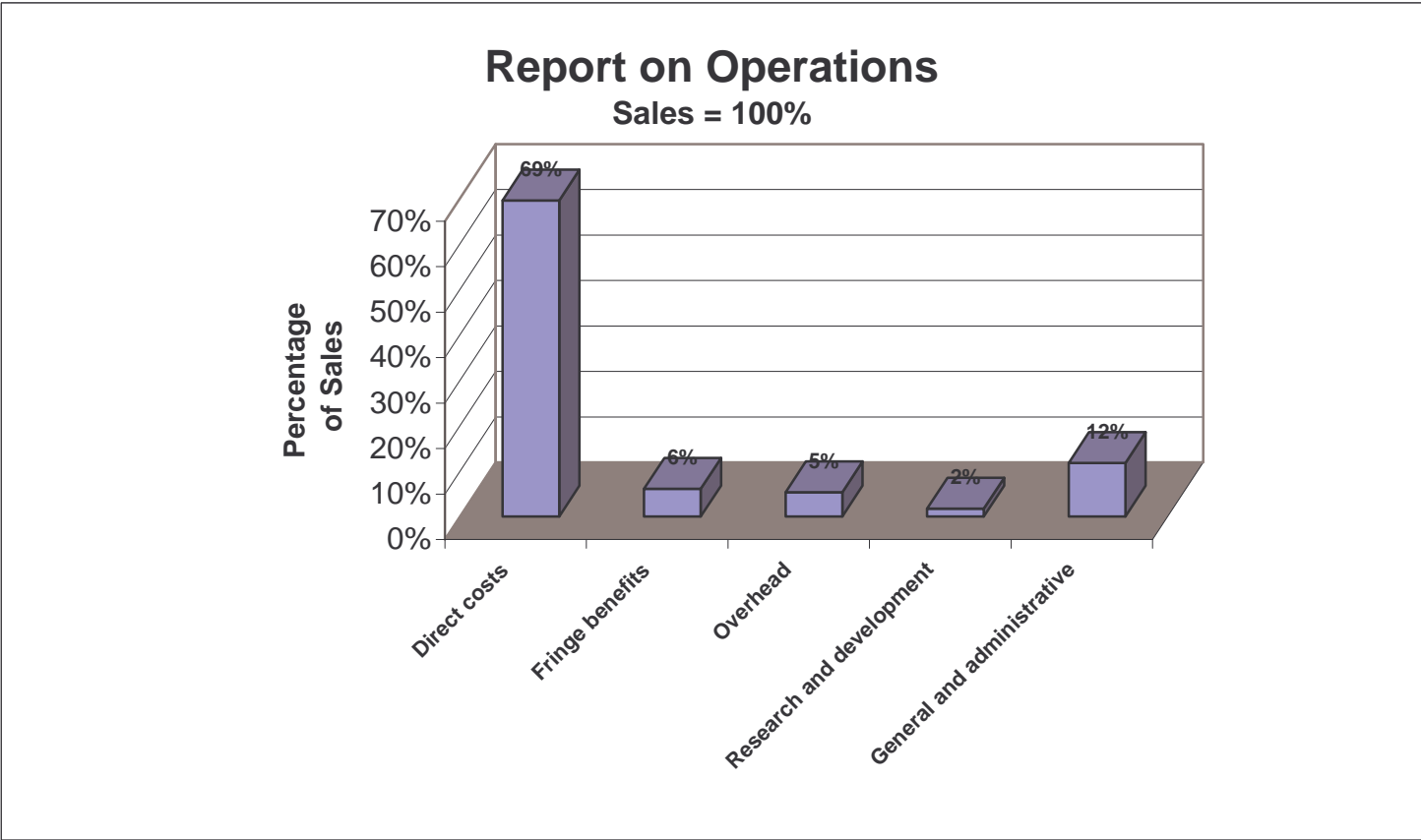
BALANCE SHEET ANALYSIS
December 31, 2003



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SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

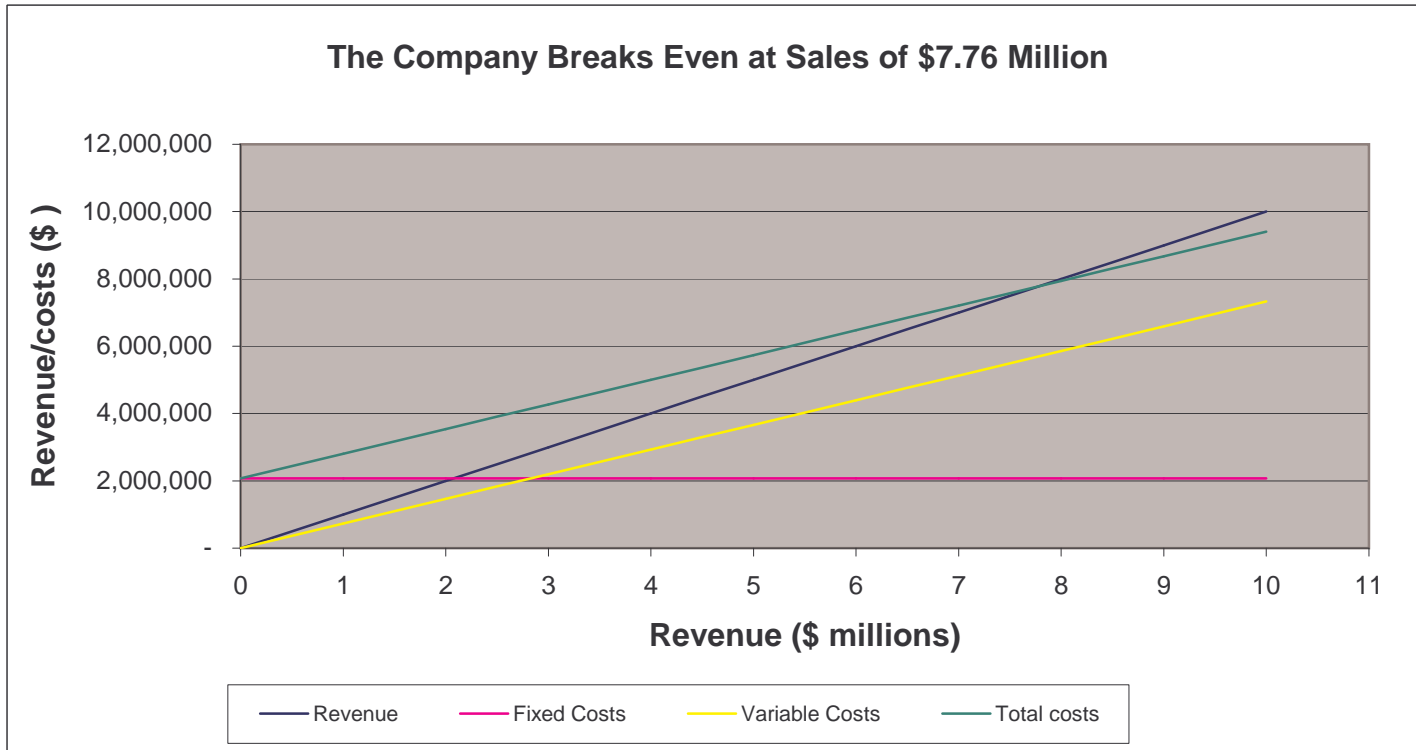
INCOME STATEMENT ANALYSIS
For the Year Ended December 31, 2003



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SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

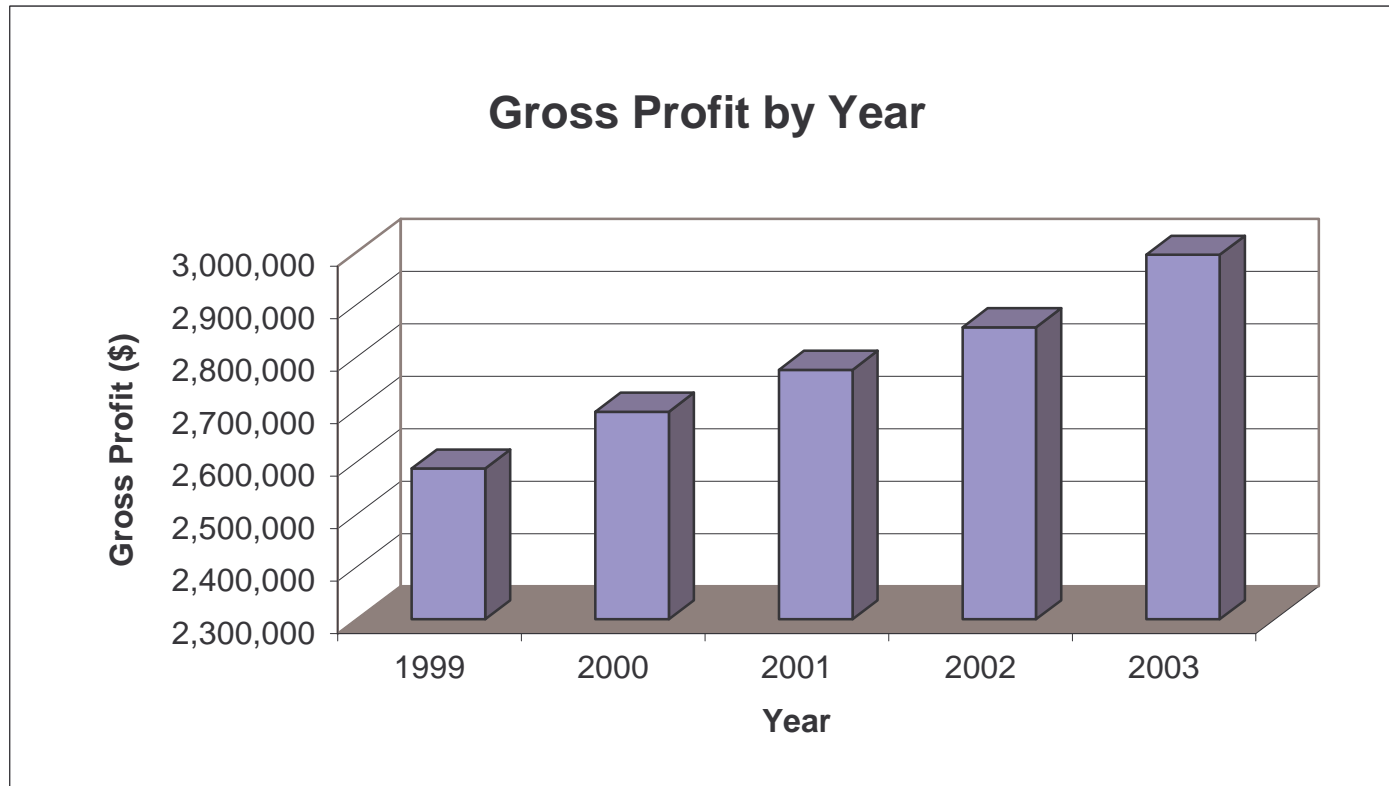
**BREAKEVEN POINT ANALYSIS
For the Year Ended December 31, 2003**



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SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

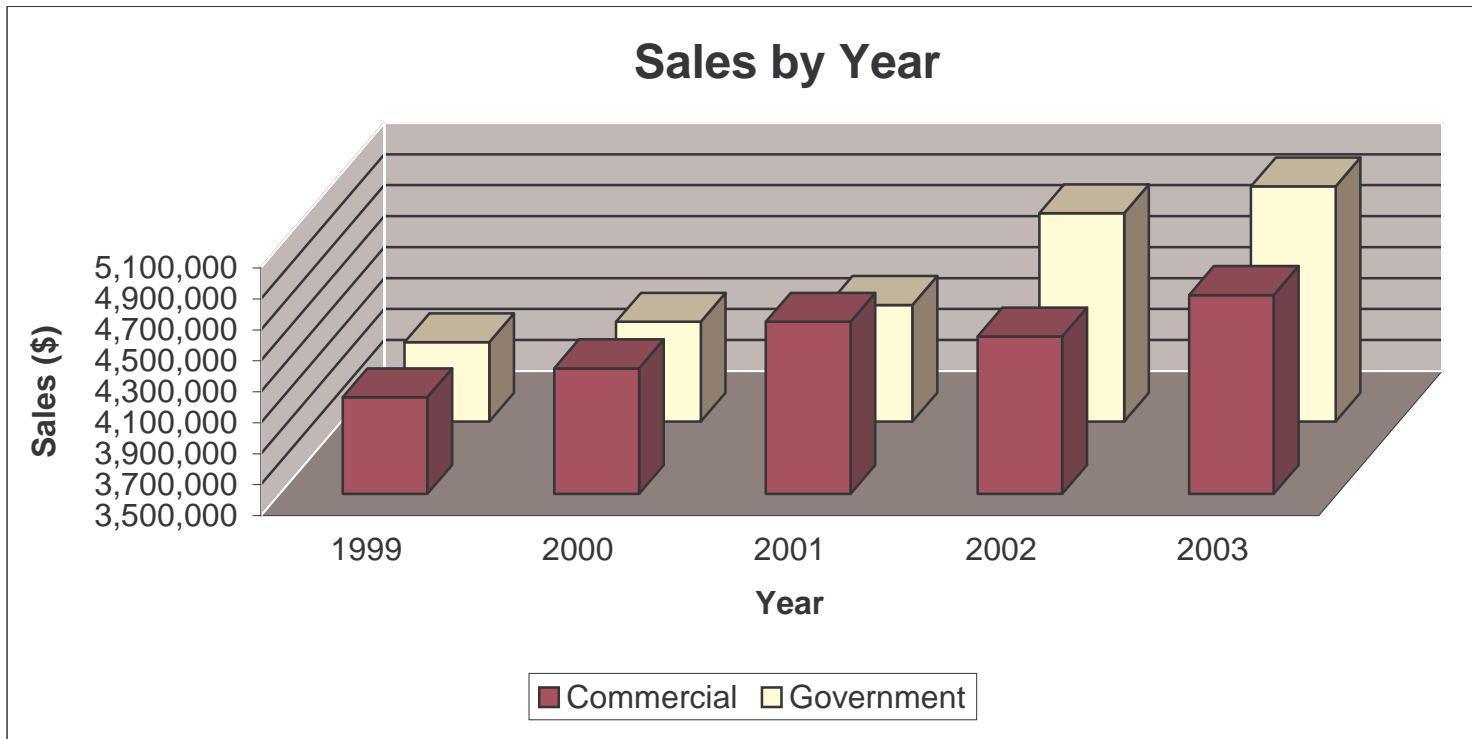
**GROSS PROFIT ANALYSIS
For Five Years Ended December 31, 2003**



SEE ACCOUNTANTS' REVIEW REPORT

SAMPLE GOVERNMENT CONTRACTOR / TECHNOLOGY, INC.

SALES BY YEAR ANALYSIS
For Five Years Ended December 31, 2003



SEE ACCOUNTANTS' REVIEW REPORT