

USAR
INC.

ANNUAL REPORT
2009

TSR AT A GLANCE

With more than 40 years experience in the information services business, TSR is positioned to fulfill virtually any information technology temporary staffing contract requirement. Extensive recruiting efforts are employed to create and maintain a database of highly qualified professionals who are well-versed in the latest technological advances. TSR's professional staff has extensive experience across a broad range of industries from telecommunications and pharmaceuticals to banking and insurance.

FINANCIAL HIGHLIGHTS

(Amounts in Thousands, Except Per Share Data)

	May 31, <u>2009</u>	May 31, <u>2008</u>	May 31, <u>2007</u>	May 31, <u>2006</u>	May 31, <u>2005</u>
Revenue	\$ 42,801	\$ 51,723	\$ 49,689	\$ 48,109	\$ 51,444
Income From Operations	998	1,971	1,925	1,709	3,635
Net Income	621	1,276	1,393	1,214	2,145
Basic and Diluted Net Income Per Common Share..	0.15	0.28	0.30	0.27	0.47
Working Capital	12,288	12,693	12,815	12,368	14,391
Total Assets	15,387	17,642	18,059	18,635	18,531
Stockholders' Equity.....	12,400	13,767	13,952	14,021	14,589
Book Value Per Common Share	3.06	3.01	3.05	3.07	3.19
Cash Dividends Declared Per Common Share.....	\$ 0.10	\$ 0.32	\$ 0.32	\$ 0.32	\$ 0.60

LETTER FROM THE CHAIRMAN

Dear Stockholders:

The effects from the financial crisis that started last October upon the market at large, TSR, and our competitors are still being felt, but conditions are slowly improving. Customers are now gradually resuming hiring programmers for temporary assignments which, as you know, is the segment of the IT industry in which we specialize.

Many corporations are still cutting costs wherever possible, and the ramifications of their reluctance to spend include lower profit margins for us. This naturally has had an adverse effect on TSR net income. One of the main reasons we have been able to continue to be profitable, although at a reduced rate for the past year, is the quality of our sales force and recruiters.

TSR continues to focus on balancing our sales costs, which are at or near historical highs as a percentage of revenues, against our mission to acquire and serve customers in this highly competitive market. In last year's annual letter, I stated that we hoped that by hiring experienced salespeople, we would be able to forge through the economic challenges to produce a reasonable amount of new business. Despite our sales force's best efforts, incremental sales gains have not been forthcoming, forcing us to reduce our team.

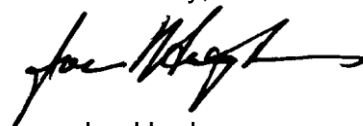
This experience has caused us to review further new business developments. TSR has determined to delay engaging in business development efforts aimed at obtaining new business and market share due to the unacceptably high costs in the current economic environment. When we become confident that these difficult and unusual times are behind us, we will once again hire the best salespeople available.

What will not change is TSR's management focus on intensely serving our clients' needs and expanding our franchise by winning over new customers. We know all too well that obtaining a reasonable number of new customers each year is essential for growth and stability. We also know from our long history that it's the nature of our business to have some customer attrition over time for a variety of reasons.

Overall, I want you to know we are confident of our long-term success, for as I mentioned previously, we have a first-class team of salespeople and recruiters. We also have a seasoned and proven management team. In addition we are a fiscally conservative company with a very strong balance sheet that enables us to withstand prolonged poor economic periods.

In closing, I want to thank you for your continued support.

Sincerely,

A handwritten signature in black ink, appearing to read "Joe Hughes", with a long horizontal flourish extending to the right.

Joe Hughes

TSR INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
May 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 4,075,213	\$ 1,588,443
Marketable securities	4,509,346	6,459,832
Accounts receivable:		
Trade, net of allowance for doubtful accounts		
of \$302,000 in 2009 and \$326,000 in 2008	6,345,374	8,176,936
Other	<u>20,580</u>	<u>52,375</u>
	6,365,954	8,229,311
Prepaid expenses	72,429	53,788
Prepaid and recoverable income taxes	101,791	48,015
Deferred income taxes	<u>133,000</u>	<u>135,000</u>
Total Current Assets	<u>15,257,733</u>	<u>16,514,389</u>
Equipment and leasehold improvements, at cost:		
Equipment	237,966	228,329
Furniture and fixtures	117,389	112,196
Automobiles	19,665	19,665
Leasehold improvements	<u>60,058</u>	<u>60,058</u>
	435,078	420,248
Less accumulated depreciation and amortization	<u>415,963</u>	<u>396,963</u>
	19,115	23,285
Marketable securities	-	999,648
Other assets	49,653	49,653
Deferred income taxes	<u>61,000</u>	<u>55,000</u>
Total Assets	<u>\$ 15,387,501</u>	<u>\$ 17,641,975</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts and other payables	\$ 274,284	\$ 313,157
Accrued and other current liabilities:		
Salaries, wages and commissions	1,191,057	1,736,285
Legal and professional fees	-	88,921
Other	<u>56,298</u>	<u>94,358</u>
	1,247,355	1,919,564
Advances from customers	<u>1,447,740</u>	<u>1,589,087</u>
Total Current Liabilities	<u>2,969,379</u>	<u>3,821,808</u>
Minority interest	17,636	53,533
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$1.00 par value, authorized 1,000,000 shares; none issued	-	-
Common stock, \$.01 par value, authorized 25,000,000 shares;		
issued 6,228,326 shares; 4,050,488 and 4,568,012 outstanding	62,283	62,283
Additional paid-in capital	5,071,727	5,071,727
Retained earnings	<u>20,517,707</u>	<u>20,663,925</u>
	25,651,717	25,797,935
Less: Treasury stock, 2,177,838 and 1,660,314 shares, at cost	<u>13,251,231</u>	<u>12,031,301</u>
Total Stockholders' Equity	<u>12,400,486</u>	<u>13,766,634</u>
Total Liabilities and Stockholders' Equity	<u>\$ 15,387,501</u>	<u>\$ 17,641,975</u>

TSR INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
Years ended May 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Revenue, net	\$ 42,801,340	\$ 51,722,850
Cost of sales	35,117,972	42,305,271
Selling, general and administrative expenses	<u>6,685,081</u>	<u>7,447,048</u>
	<u>41,803,053</u>	<u>49,752,319</u>
Income from operations	<u>998,287</u>	<u>1,970,531</u>
Other income (expense):		
Interest and dividend income	149,466	361,082
Realized and unrealized gain (loss) from marketable securities, net.....	(5,968)	800
Minority interest in subsidiary operating profits	<u>(47,393)</u>	<u>(85,279)</u>
	<u>96,105</u>	<u>276,603</u>
Income before income taxes	1,094,392	2,247,134
Provision for income taxes	<u>473,000</u>	<u>971,000</u>
Net income	\$ <u>621,392</u>	\$ <u>1,276,134</u>
Basic and diluted net income per common share	\$ <u>0.15</u>	\$ <u>0.28</u>
Weighted average number of basic and diluted common shares outstanding	<u>4,235,723</u>	<u>4,568,012</u>

TSR INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years ended May 31, 2009 and 2008

	Shares of common stock	Common stock	Additional paid-in capital	Retained earnings	Treasury stock	Total stock- holders' equity
Balance at May 31, 2007	6,228,326	\$ 62,283	\$ 5,071,727	\$ 20,849,555	\$(12,031,301)	\$ 13,952,264
Net Income.....	-	-	-	1,276,134	-	1,276,134
Cash Dividends Paid.....	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,461,764)</u>	<u>-</u>	<u>(1,461,764)</u>
Balance at May 31, 2008	6,228,326	62,283	5,071,727	20,663,925	(12,031,301)	13,766,634
Net Income.....	-	-	-	621,392	-	621,392
Cash Dividends Paid.....	-	-	-	(767,610)	-	(767,610)
Purchases of Treasury Stock.....	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,219,930)</u>	<u>(1,219,930)</u>
Balance at May 31, 2009	<u>6,228,326</u>	<u>\$ 62,283</u>	<u>\$ 5,071,727</u>	<u>\$ 20,517,707</u>	<u>\$(13,251,231)</u>	<u>\$ 12,400,486</u>

TSR INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended May 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:		
Net Income	\$ 621,392	\$ 1,276,134
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	19,000	24,446
Realized and unrealized loss (gain) from marketable securities, net.....	5,968	(800)
Deferred income taxes	(4,000)	17,000
Minority interest in subsidiary operating profits.....	47,393	85,279
Changes in operating assets and liabilities:		
Accounts receivable-trade.....	1,831,562	(20,285)
Other receivables.....	31,795	46,640
Prepaid expenses.....	(18,641)	1,140
Prepaid and recoverable income taxes	(53,776)	105,603
Accounts payable and accrued expenses	(711,082)	(265,186)
Advances from customers.....	<u>(141,347)</u>	<u>(2,237)</u>
Net cash provided by operating activities.....	<u>1,628,264</u>	<u>1,267,734</u>
Cash flows from investing activities:		
Proceeds from maturities and sales of marketable securities	10,403,782	10,777,957
Purchases of marketable securities.....	(7,459,616)	(10,845,061)
Purchases of equipment and leasehold improvements	<u>(14,830)</u>	<u>(1,441)</u>
Net cash provided by (used in) investing activities.....	<u>2,929,336</u>	<u>(68,545)</u>
Cash flows from financing activities:		
Distribution to minority interest.....	(83,290)	(49,246)
Cash dividends paid	(767,610)	(1,461,764)
Purchases of treasury stock.....	<u>(1,219,930)</u>	<u>-</u>
Net cash used in financing activities.....	<u>(2,070,830)</u>	<u>(1,511,010)</u>
Net increase (decrease) in cash and cash equivalents.....	2,486,770	(311,821)
Cash and cash equivalents at beginning of year	<u>1,588,443</u>	<u>1,900,264</u>
Cash and cash equivalents at end of year.....	\$ <u>4,075,213</u>	\$ <u>1,588,443</u>
Supplemental disclosures of cash flow:		
Income taxes paid.....	\$ <u>531,000</u>	\$ <u>848,000</u>

TSR INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
May 31, 2009 and 2008

(1) Summary of Significant Accounting Policies

(a) Business, Nature of Operations and Customer Concentrations

TSR, Inc. and subsidiaries (“the Company”) are primarily engaged in providing contract computer programming services to commercial customers and state and local government agencies located primarily in the Metropolitan New York area. The Company provides its clients with technical computer personnel to supplement their in-house information technology capabilities. In fiscal 2009, one customer accounted for more than 10% of the Company’s consolidated revenue, constituting 28.3%. In fiscal 2008, two customers accounted for more than 10% of the Company’s consolidated revenue, constituting 13.5% and 12.2%, respectively. The accounts receivable associated with the Company’s largest customer was \$1,906,000 and \$1,368,000 at May 31, 2009 and 2008, respectively. The accounts receivable associated with the Company’s second largest customer was \$917,000 at May 31, 2008. The Company operates in one business segment, computer programming services.

(b) Principles of Consolidation

The consolidated financial statements include the accounts of TSR, Inc. and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

(c) Revenue Recognition

The Company’s contract computer programming services are generally provided under time and materials arrangements with its customers. Revenue is recognized in accordance with Staff Accounting Bulletin (SAB) 104, “Revenue Recognition”, when persuasive evidence of an arrangement exists, the services have been rendered, the price is fixed or determinable, and collectability is reasonably assured. These conditions occur when a customer agreement is effected and the consultant performs the authorized services. Advances from customers represent amounts received from customers prior to the Company’s completion of the related services and credit balances from overpayments.

Reimbursements received by the Company for out-of-pocket expenses are characterized as revenue in accordance with Emerging Issues Task Force (EITF) Issue 01-14 “Income Statement Characterization of Reimbursements Received for ‘Out-of-Pocket’ Expenses Incurred.”

(d) Cash and Cash Equivalents

The Company considers short-term highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents. Cash and cash equivalents were comprised of the following as of May 31, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
Cash in banks	\$ 2,008,349	\$ 394,987
Money market funds.....	<u>2,066,864</u>	<u>1,193,456</u>
	<u>\$ 4,075,213</u>	<u>\$1,588,443</u>

(e) Marketable Securities

In fiscal 2009, the Company adopted the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 157 “Fair Value Measurements” (“SFAS No. 157”). Using the provisions within SFAS No. 157, the Company has characterized its investments in marketable securities, based on the priority of the inputs used to value the investments, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1), and lowest priority to unobservable inputs (Level 3). If the inputs used to measure the investments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

TSR INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
May 31, 2009 and 2008

Investments recorded in the accompanying consolidated balance sheets are categorized based on the inputs to valuation techniques as follows:

- Level 1 - These are investments where values are based on unadjusted quoted prices for identical assets in an active market the Company has the ability to access.
- Level 2 - These are investments where values are based on quoted market prices that are not active or model derived valuations in which all significant inputs are observable in active markets.
- Level 3 - These are investments where values are derived from techniques in which one or more significant inputs are unobservable.

The following are the major categories of assets measured at fair value on a recurring basis during the fiscal year ended May 31, 2009 using quoted prices in active markets for identical assets (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3):

May 31, 2009	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
US Treasury securities	\$ 2,497,133	\$ -	\$ -	\$ 2,497,133
Certificates of deposit	-	1,999,637	-	1,999,637
Equity securities	12,576	-	-	12,576
	<u>\$ 2,509,709</u>	<u>\$ 1,999,637</u>	<u>\$ -</u>	<u>\$ 4,509,346</u>

Based upon the Company's intent and ability to hold its US Treasury securities to maturity (which maturities range up to twenty-four months at purchase), such securities have been classified as held-to-maturity and are carried at amortized cost, which approximates market value. The Company's equity securities are classified as trading securities, which are carried at fair value, as determined by quoted market prices, which is Level 1 input, as established by the fair value hierarchy under SFAS No. 157. The related unrealized gains and losses are included in earnings. The Company's marketable securities at May 31, 2009 and 2008 are summarized as follows:

	<u>Amortized Cost</u>	<u>Gross Unrealized Holding Gains</u>	<u>Gross Unrealized Holding Losses</u>	<u>Recorded Value</u>
<u>Current</u>				
2009: US Treasury securities	\$ 2,497,133	\$ -	\$ -	\$ 2,497,133
Certificates of deposit	1,999,637	-	-	1,999,637
Equity securities	16,866	-	4,290	12,576
	<u>\$ 4,513,636</u>	<u>\$ -</u>	<u>\$ 4,290</u>	<u>\$ 4,509,346</u>
<u>Long Term</u>				
US Treasury securities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
<u>Current</u>				
2008: US Treasury securities	\$ 6,441,288	\$ -	\$ -	\$ 6,441,288
Equity securities	16,866	1,678	-	18,544
	<u>\$ 6,458,154</u>	<u>\$ 1,678</u>	<u>\$ -</u>	<u>\$ 6,459,832</u>
<u>Long Term</u>				
US Treasury securities	<u>\$ 999,648</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 999,648</u>

The Company's investments in marketable securities consist primarily of investments in US Treasury securities and certificates of deposit. Market values were determined for each individual security in the investment portfolio. When evaluating the investments for other-than-temporary impairment, the Company reviews factors such as length of time and extent to which fair value has been below cost basis, the financial condition of the issuer, and the Company's ability and intent to hold the investment for a period of time, which may be sufficient for anticipated recovery in market values.

TSR INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
May 31, 2009 and 2008

(f) Accounts Receivable and Credit Policies:

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, management considers many factors in estimating its general allowance, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, management may adjust its assumptions for anticipated changes in any of those or other factors expected to affect collectability.

(g) Depreciation and Amortization

Depreciation and amortization of equipment and leasehold improvements has been computed using the straight-line method over the following useful lives:

Equipment	3 years
Furniture and fixtures.....	3 years
Automobiles	3 years
Leasehold improvements	Lesser of lease term or useful life

(h) Net Income Per Common Share

Basic net income per common share is computed by dividing income available to common stockholders (which for the Company equals its net income) by the weighted average number of common shares outstanding, and diluted net income per common share adds the dilutive effect of stock options and other common stock equivalents, if any. The Company had no stock options or other common stock equivalents outstanding during the fiscal years ended May 31, 2009 or 2008.

(i) Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial reporting and tax bases of the Company's assets and liabilities at enacted rates expected to be in effect when such amounts are realized or settled. The effect of enacted tax law or rate changes is reflected in income in the period of enactment.

(j) Fair Value of Financial Instruments

Statement of Financial Accounting Standards No. 107, "Disclosures About Fair Value of Financial Instruments" requires disclosure of the fair value of certain financial instruments. For cash and cash equivalents, accounts receivable, accounts and other payables, accrued liabilities and advances from customers, the amounts presented in the consolidated financial statements approximate fair value because of the short-term maturities of these instruments. The fair value of marketable securities is based upon quoted market values at the end of a period.

(k) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Such estimates include, but are not limited to provisions for doubtful accounts receivable and assessments of the recoverability of the Company's deferred tax assets. Actual results could differ from those estimates.

(l) Long-Lived Assets

The Company reviews its long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the sum of the expected cash flows undiscounted and without interest, is less than the carrying amount of the asset, an impairment loss is recognized for the amount by which the carrying amount of the asset exceeds its fair value.

(m) Comprehensive Income

The Company's net income equaled comprehensive income in both fiscal 2009 and 2008.

(n) Stock Options

The Company had one stock-based employee compensation plan which expired on April 30, 2007. Effective June 1, 2006, the Company accounted for all transactions under which employees receive shares of stock or other equity instruments in the Company in accordance with the revised provisions of Statement of Financial Accounting Standards No. 123, "Share-Based Payment", ("SFAS 123 (R)"), which requires that the fair market value of all share based payment transactions be recognized in the financial statements. SFAS 123 (R) establishes fair value as the measurement objective in accounting for share based payment arrangements and requires all entities to apply a fair value based measurement method in accounting for share based transactions with employees except for equity instruments held by employee share ownership plans. The Company adopted SFAS 123 (R) at the beginning of fiscal 2007. The Company has not issued any share based payments in fiscal 2009 or 2008.

TSR INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
May 31, 2009 and 2008

(o) Impact of New Accounting Standards

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"), which, among other requirements, defines fair value, establishes a framework for measuring fair value, and expands disclosures about the use of fair value to measure assets and liabilities. SFAS No. 157 prescribes a single definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. For financial instruments and certain nonfinancial assets and liabilities that are recognized or disclosed at fair value on a recurring basis at least annually, SFAS No. 157 is effective beginning the first fiscal year that begins after November 15, 2007, which corresponds to the Company's fiscal year beginning June 1, 2008. For all other nonfinancial assets and liabilities, the effective date of SFAS No. 157 has been delayed to the first fiscal year beginning after November 15, 2008, which corresponds to the Company's fiscal year beginning June 1, 2009. The Company is still determining the effect SFAS No. 157 will have on its consolidated financial statements, but it currently does not expect the effect to be material.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities – including an amendment to FASB Statement No. 115" ("SFAS No. 159"). SFAS No. 159 permits entities to elect to measure many financial instruments and certain other items at fair value. Upon adoption of SFAS No. 159, an entity may elect the fair value option for eligible items that exist at the adoption date. Subsequent to the initial adoption, the election of the fair value option should only be made at initial recognition of the asset or liability or upon a re-measurement event that gives rise to new-basis accounting. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value nor does it eliminate disclosure requirements included in other accounting standards. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The adoption of SFAS No. 159 did not have a material impact on the Company's consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (R), "Business Combinations" ("SFAS No. 141(R)"), and SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements" ("SFAS No. 160"). SFAS No. 141 (R) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. SFAS No. 160 clarifies that a noncontrolling interest in a subsidiary should be reported as equity in the consolidated financial statements. The calculation of earnings per share will continue to be based on income amounts attributable to the parent. SFAS No. 141 (R) and SFAS No. 160 are effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. The Company does not expect the adoption of SFAS No. 141 (R) and SFAS No. 160 to have a material impact on its consolidated financial statements.

In June 2009, the FASB issued SFAS No. 165, "Subsequent Events". SFAS No. 165 incorporates the subsequent events guidance contained in the auditing standards literature into authoritative accounting literature. It also requires entities to disclose the date through which they have evaluated subsequent events and whether the date corresponds with the release of their financial statements. SFAS No. 165 is effective for all interim and annual periods ending after June 15, 2009. The Company does not expect the adoption of SFAS No. 165 to have a material impact on its consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, "The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No. 162". The FASB Accounting Standards Codification (the "Codification") will become the source of authoritative accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Codification, which changes the referencing of financial standards, is effective for interim or annual financial periods ending after September 15, 2009. The Codification is not intended to change or alter existing U.S. GAAP.

(p) Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities and accounts receivable. The Company places its cash equivalents with high-credit quality financial institutions and brokerage houses. The Company has substantially all of its cash in three bank accounts. At times, such amounts may exceed Federally insured limits. At May 31, 2009, there were no cash balances in excess of Federally insured limits. The Company holds its marketable securities, which consist primarily of United States Treasury Securities, directly with the Treasury and in brokerage accounts. The Company has not experienced losses in any such accounts. The Company's accounts receivable represent approximately 55 accounts with open balances of which, the largest customer, as a percentage of revenue, consisted of 30.0% of the net accounts receivable balance at May 31, 2009.

TSR INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
May 31, 2009 and 2008

(2) Income Taxes

A reconciliation of the provisions for income taxes computed at the Federal statutory rates for fiscal 2009 and 2008 to the reported amounts is as follows:

	2009		2008	
	Amount	%	Amount	%
Amounts at statutory Federal tax rate	\$ 372,000	34.0%	\$ 764,000	34.0%
State and local taxes, net of Federal income tax effect.....	91,000	8.3	168,000	7.5
Non-deductible expenses, and other	10,000	0.9	39,000	1.7
	<u>\$ 473,000</u>	<u>43.2%</u>	<u>\$ 971,000</u>	<u>43.2%</u>

The components of the provision for income taxes are as follows:

	Federal	State	Total
2009: Current.....	\$ 341,000	\$ 136,000	\$ 477,000
Deferred.....	(4,000)	-	(4,000)
	<u>\$ 337,000</u>	<u>\$ 136,000</u>	<u>\$ 473,000</u>
2008: Current.....	\$ 704,000	\$ 250,000	\$ 954,000
Deferred	12,000	5,000	17,000
	<u>\$ 716,000</u>	<u>\$ 255,000</u>	<u>\$ 971,000</u>

The tax effects of temporary differences that give rise to significant portions of the deferred income tax assets at May 31, 2009 and 2008 are as follows:

	2009	2008
Allowance for doubtful accounts receivable.....	\$ 133,000	\$ 135,000
Equipment and leasehold improvement depreciation and amortization.....	25,000	15,000
Acquired client relationships	36,000	40,000
Total deferred income tax assets.....	<u>\$ 194,000</u>	<u>\$ 190,000</u>

The Company believes that it is more likely than not that it will realize the benefits of its deferred tax assets based primarily on the Company's history of and projections for taxable income in the future.

(3) Line of Credit

The Company has an available line of credit of \$5,000,000 with a major money center bank through October 31, 2009. As of May 31, 2009, no amounts were outstanding under this line of credit. The rate of interest on amounts drawn against the line of credit will be either the Eurodollar Rate plus 1% or the Prime Rate, determined at the time of the advance.

(4) Commitments and Contingencies

A summary of noncancellable long-term operating lease commitments for facilities as of May 31, 2009 follows:

Fiscal Year	Amount
2010	\$ 364,000
2011	332,000
2012	297,000
2013	181,000
2014	39,000
Total	<u>\$ 1,213,000</u>

Total rent expenses under all lease agreements amounted to \$346,000 and \$353,000 in fiscal 2009 and 2008, respectively.

From time to time, the Company is party to various lawsuits, some involving substantial amounts. Management is not aware of any lawsuits that would have a material adverse impact on the consolidated financial position of the Company.

(5) Stockholder Equity

During the year ended May 31, 2009, the Company purchased a total of 517,524 shares of its common stock for \$1,219,930. This consisted of 61,001 shares purchased in various transactions on the open market for \$169,927 under a previously announced repurchase plan of 300,000 shares and an additional 456,523 shares purchased in a private transaction for \$1,050,003 in October 2008. The Company has not made any purchases under its repurchase plan since September 2008.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the Company's consolidated financial statements and notes thereto presented elsewhere in this report.

Results of Operations

The following table sets forth for the periods indicated certain financial information derived from the Company's consolidated statements of income. There can be no assurance that historical trends in operating results will continue in the future:

	Year Ended May 31, (Dollar Amounts in Thousands)			
	<u>2009</u>	<u>% of</u>	<u>2008</u>	<u>% of</u>
	<u>Amount</u>	<u>Revenue</u>	<u>Amount</u>	<u>Revenue</u>
Revenue	\$ 42,801	100.0%	\$ 51,723	100.0%
Cost of Sales	<u>35,118</u>	<u>82.1</u>	<u>42,305</u>	<u>81.8</u>
Gross Profit.....	<u>7,683</u>	<u>17.9</u>	9,418	18.2
Selling, General and Administrative Expenses....	<u>6,685</u>	<u>15.6</u>	<u>7,447</u>	<u>14.4</u>
Income from Operations.....	<u>998</u>	<u>2.3</u>	1,971	3.8
Other Income, Net.....	<u>96</u>	<u>0.2</u>	<u>276</u>	<u>0.6</u>
Income Before Income Taxes.....	<u>1,094</u>	<u>2.5</u>	2,247	4.4
Provision for Income Taxes.....	<u>473</u>	<u>1.1</u>	<u>971</u>	<u>1.9</u>
Net Income	<u>\$ 621</u>	<u>1.4%</u>	\$ <u>1,276</u>	<u>2.5%</u>

Revenue

Revenue consists primarily of revenue from computer programming consulting services. Revenue for the fiscal year ended May 31, 2009 decreased \$8,922,000 or 17.2% from fiscal 2008. The average number of consultants on billing with customers decreased from approximately 332 for the fiscal year ended May 31, 2008 to 264 for the fiscal year ended May 31, 2009. The continuing impact of the current economic environment has significantly decreased the number of consultants on billing with customers and also decreased the opportunities to place new consultants on billing with customers. The revenue decrease is also the result of the continued reduction in consultants placed with AT&T and lower billing rates caused by discounts and other rate reductions instituted by customers.

As a result of the merger of AT&T with SBC Communications, Inc., the Company experienced a decrease in new placements with AT&T beginning in the second quarter of fiscal 2007. This has reduced the number of consultants on billing with AT&T from 100 at August 31, 2006 to 45 at May 31, 2008 and to 14 at May 31, 2009. The Company expects that these changes will continue to impact the Company's business relationship with AT&T, resulting in few opportunities to place new consultants at AT&T.

The Company's revenue from programmers on billing continue to be affected by discounts, such as prompt payment and volume discounts, required by major customers as a condition to remaining on their approved vendor lists and the reduction in the number of vendors on the approval vendor lists to increase pricing competition among the remaining vendors. In addition, most of the Company's major customers have retained third parties to provide vendor management services and centralize the consultant hiring process. Under this system, the third

party retains the Company to provide contract computer programming services, the Company bills the third party and the third party bills the ultimate customer. This process has weakened the relationships the Company has built with its client contacts, the project managers, who the Company would normally work directly with to place consultants. Instead, the Company is required to interface with the vendor management provider, making it more difficult to maintain its relationships with its customers and preserve and expand its business. These changes have also reduced the Company's profit margins because the vendor management company is retained for the purpose of keeping costs down for the end client and receives a processing fee which is deducted from the payment to the Company. Revenue has also been impacted by the increased use of offshore development companies, particularly in India, over the past few years to provide technology related work and projects. The Company is unable to predict the long-term effects of these changes.

As a result of the current economic downturn and, specifically, the impact of the adverse conditions in the credit markets on the financial services industry, the Company has experienced a decrease in the number of consultants on billing with customers as a result of decreased IT spending. These economic conditions have also reduced the opportunities to place new consultants on billing with customers. The Company expects that these conditions will continue to affect the number of consultants on billing with customers and the Company's revenue.

The Company provided services to Lehman Brothers Holdings, Inc. ("LBHI") through its contract with Beeline.com, Inc. ("Beeline"), a vendor management company. LBHI filed a petition under Chapter 11 of the U.S. Bankruptcy Code on September 15, 2008. The Company

TSR INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

has received payment in full for amounts due for services rendered through the date of the bankruptcy filing. Following the bankruptcy filing, the consultants on billing with LBHI decreased from 13 as of August 31, 2008 to 3 as of May 31, 2009. The Company cannot determine the impact the bankruptcy filing and purchase of Lehman Brothers, Inc. ("LBI") by Barclays Capital, Inc. will have on the remaining consultants on billing with LBI and its affiliates. LBHI and its subsidiaries constituted approximately 6% of the Company's revenue in fiscal 2008 and 4% in fiscal 2009.

Cost of Sales

Cost of sales decreased by \$7,187,000 or 17.0%, in fiscal 2009 from fiscal 2008. Cost of sales as a percentage of revenue increased to 82.1% in fiscal 2009 from 81.8% in fiscal 2008. The decrease in cost of sales resulted primarily from decreased revenue. The increase in cost of sales as a percentage of revenue is due to additional mandatory discount and rate reduction programs, as discussed above under "Revenue".

Selling, General and Administrative Expenses

Selling, general and administrative expenses consist primarily of expenses relating to account executives, technical recruiters, facilities costs, management and corporate overhead. These expenses decreased \$762,000, or 10.2%, to \$6,685,000 in fiscal 2009 from \$7,447,000 in fiscal 2008. This decrease was primarily attributable to a decrease in the number of technical recruiters and account executives. Technical recruiters and account executives have been terminated in order to lessen the impact of the Company's reduced level of business activity.

Other Income

Fiscal 2009 other income resulted primarily from interest and dividend income of \$149,000, which decreased by \$212,000 from the level realized in 2008 due to lower rates of interest earned on the Company's US Treasury securities and money market accounts.

Income Taxes

The effective income tax rate remained at 43.2% in both fiscal 2009 and fiscal 2008.

Net Income

Net income decreased \$655,000 or 51.3% in fiscal 2009 from fiscal 2008. Net income decreased primarily due to lower revenue from a decreased number of consultants on billing with clients and lower interest income earned on the Company's US Treasury securities and money market accounts.

Liquidity, Capital Resources and Changes in Financial Condition

The Company expects that cash flow generated from operations together with its available cash and marketable securities will be sufficient to provide the Company with adequate resources to meet its liquidity requirements for the next 12 months.

At May 31, 2009, the Company had working capital (total current assets in excess of total current liabilities) of \$12,288,000 including cash and cash equivalents of \$4,075,000 as compared to working capital of \$12,693,000 including cash and cash equivalents of \$1,588,000 at May 31, 2008. The Company's working capital also included \$4,509,000 and \$6,460,000 of marketable securities with maturities of less than one year at May 31, 2009 and 2008, respectively. The majority of the decrease in working capital occurred due to purchases of treasury stock of \$1,220,000 and cash dividends paid exceeding net income by \$146,000, offset to some extent by the reclassification of \$1,000,000 of marketable securities to current assets.

Net cash flow of \$1,628,000 was provided by operations during fiscal 2009 as compared to \$1,268,000 of net cash flow from operations in fiscal 2008. The cash provided by operations for fiscal 2009 primarily resulted from net income of \$621,000 and a decrease in accounts receivable of \$1,832,000. The cash provided by operations for fiscal 2008 primarily resulted from net income of \$1,276,000 and a decrease in accounts payable and accrued expenses of \$265,000.

Net cash provided by investing activities amounted to \$2,929,000 for fiscal 2009, compared to \$69,000 in net cash used in investing activities in fiscal 2008. The net cash provided by investing activities in fiscal 2009 primarily resulted from not reinvesting maturities of treasury securities. The net cash used in investing activities in fiscal 2008 primarily resulted from higher prices paid for reinvesting in treasury securities.

Net cash used in financing activities during the fiscal year ended May 31, 2009 resulted from purchases of treasury securities of \$1,220,000, cash dividends paid of \$768,000 and distributions of \$83,000 to the minority interest. The purchases of treasury stock consisted of \$1,050,000 in a private transaction and \$170,000 in open market transactions. The Board of Directors of the Company approved a plan in December 2007 authorizing the repurchase of shares of common stock and approximately 239,000 shares remain available for purchase under this previously announced plan. The Company has not made any purchases under this plan since September 2008. The Company does not intend to make further purchases under this plan unless there is a change in the market for the Company's common stock. Net cash used in financing activities during the fiscal year ended May 31, 2008 resulted primarily from cash dividends paid of \$1,462,000 and distributions of \$49,000 to the minority interest. The Board of Directors determined to suspend the payment of further dividends effective after the dividend paid February 9, 2009 for the second quarter of fiscal 2009. The Board of Directors may reevaluate the Company's dividend policy once the economic conditions stabilize.

The Company's capital resource commitments at May 31, 2009 consisted of lease obligations on its branch and corporate facilities. The Company intends to finance these lease commitments from cash flow provided by operations, available cash and short-term marketable securities.

TSR INC. AND SUBSIDIARIES
MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND
RESULTS OF OPERATIONS

The Company’s cash and marketable securities were sufficient to enable it to meet its liquidity requirements during fiscal 2009. The Company has available a revolving

line of credit of \$5,000,000 with a major money center bank through October 31, 2009. As of May 31, 2009, no amounts were outstanding under this line of credit.

Tabular Disclosure of Contractual Obligations
Payments Due by Period

<u>Contractual Obligations</u>	<u>Total</u>	<u>Less than 1 Year</u>	<u>1-3 Years</u>	<u>3-5 Years</u>	<u>More than 5 Years</u>
Operating Leases.....	\$ 1,213,000	\$ 364,000	\$ 629,000	\$ 220,000	\$ -
Employment Agreements....	<u>725,000</u>	<u>375,000</u>	<u>350,000</u>	<u>-</u>	<u>-</u>
Totals.....	\$ <u>1,938,000</u>	\$ <u>739,000</u>	\$ <u>979,000</u>	\$ <u>220,000</u>	\$ <u>-</u>

Impact of New Accounting Standards

In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements” (“SFAS No. 157”), which, among other requirements, defines fair value, establishes a framework for measuring fair value, and expands disclosures about the use of fair value to measure assets and liabilities. SFAS No. 157 prescribes a single definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between participants at the measurement date. For financial instruments and certain nonfinancial assets and liabilities that are recognized or disclosed at fair value on a recurring basis at least annually, SFAS No. 157 is effective beginning the first fiscal year that begins after November 15, 2007, which corresponds to the Company’s fiscal year beginning June 1, 2008. For all other nonfinancial assets and liabilities, the effective date of SFAS no. 157 has been delayed to the first fiscal year beginning after November 15, 2008, which corresponds to the Company’s fiscal year beginning June 1, 2009. The Company is still determining the effect SFAS No. 157 will have on its consolidated financial statements, but it currently does not expect the effect to be material.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities – including an amendment to FASB Statement No. 115” (“SFAS No. 159”). SFAS No. 159 permits entities to elect to measure many financial instruments and certain other items at fair value. Upon adoption of SFAS No. 159, an entity may elect the fair value option for eligible items that exist at the adoption date. Subsequent to the initial adoption, the election of the fair value option should only be made at initial recognition of the asset or liability or upon a re-measurement event that gives rise to new-basis accounting. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value nor does it eliminate disclosure requirements included in other accounting standards. SFAS No. 159 is effective for fiscal years after November 15, 2007. The adoption of SFAS No. 159 did not have a material impact on the Company’s consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (R), “Business Combinations” (“SFAS No.141(R)”), and SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements” (“SFAS No.160”). SFAS No.141 (R) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. SFAS No. 160 clarifies that a noncontrolling interest in a subsidiary should be reported as equity in the consolidated financial statements. The calculation of earnings per share will continue to be based on income amounts attributable to the parent. SFAS No. 141 (R) and SFAS No. 160 are effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. The Company does not expect the adoption of SFAS No.141 (R) and SFAS No. 160 to have a material impact on its consolidated financial statements

In June 2009, the FASB issued SFAS No. 165, “Subsequent Events”. SFAS No. 165 incorporates the subsequent events guidance contained in the auditing standards literature into authoritative accounting literature. It also requires entities to disclose the date through which they have evaluated subsequent events and whether the date corresponds with the release of their financial statements. SFAS No.165 is effective for all interim and annual periods ending after June 15, 2009. The Company does not expect the adoption of SFAS No. 165 to have a material impact on its consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, “The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No.162”. The FASB Accounting Standards Codification (the “Codification”) will become the source of authoritative U.S. accounting principles generally accepted in the United States of America (“U.S. GAAP”). The Codification, which changes the referencing of financial standards, is effective for interim or annual financial periods ending after September 15, 2009. The Codification is not intended to change or alter existing U.S. GAAP.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Critical Accounting Policies

The SEC defines "critical accounting policies" as those that require the application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The Company's significant accounting policies are described in Note 1 to its consolidated financial statements, contained elsewhere in this report. The Company believes that the following accounting policies require the application of management's most difficult, subjective or complex judgments:

Estimating Allowances for Doubtful Accounts Receivable

We perform ongoing credit evaluations of our customers and adjust credit limits based upon payment history and the customer's current credit worthiness, as determined by our review of their current credit information. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based on our historical experience, customer types, credit worthiness, economic trends and any specific customer collection issues that we have identified. While such credit losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. A significant change in the liquidity or financial position of any of our significant customers, or in their willingness to pay, could have a material adverse effect on the collectibility of our accounts receivable and our future operating results.

Valuation of Marketable Securities

The Company accounts for its marketable securities in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115 "Accounting for Certain Investments in Debt and Equity Securities." Accordingly, the Company classifies its marketable securities at acquisition as either (i) held-to-maturity, (ii) trading or (iii) available-for-sale. Based upon the Company's intent and ability to hold its US Treasury securities to maturity (which maturities range up to 24 months), such securities have been classified as held-to-maturity and are carried at amortized cost, which approximates market value. The Company's equity securities are classified as trading securities, which are carried at fair value, as determined by quoted market price, which is Level 1 input, as established by the fair value hierarchy under SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"). The related unrealized gains and losses are included in earnings.

Valuation of Deferred Tax Assets

We regularly evaluate our ability to recover the reported amount of our deferred income taxes considering several factors, including our estimate of the likelihood of the Company generating sufficient taxable income in future years during the period over which temporary differences reverse. Presently, the Company believes that it is more likely than not that it will realize the benefits of its deferred tax assets based primarily on the Company's history of and

projections for taxable income in the future. In the event that actual results differ from our estimates or we adjust these estimates in future periods, we may need to establish a valuation allowance against a portion or all of our deferred tax assets, which could materially impact our financial position or results of operations.

Forward-Looking Statements; Factors that Affect Future Results

Certain statements contained herein, including statements concerning the Company's future prospects and the Company's future cash flow requirements are forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projections in the forward-looking statements which statements involve risks and uncertainties, including but not limited to the following: the impact of current adverse conditions in the credit markets and current adverse economic conditions on the Company's business; risks relating to the competitive nature of the markets for contract computer programming services; the extent to which market conditions for the Company's contract computer consulting services will continue to adversely affect the Company's business; concentration of the Company's business with certain customers, uncertainty as to the Company's ability to maintain its relations with existing customers and expand its contract computer consulting services business; the impact of changes in the industry, such as the use of vendor management companies in connection with the consultant procurement process, the increase in customers moving IT operations offshore and other risks and uncertainties set forth in the Company's filings with the Securities and Exchange Commission. The Company is under no obligation to publicly update or revise forward-looking statements.

TSR INC. AND SUBSIDIARIES
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
TSR, Inc.
Hauppauge, New York

We have audited the accompanying consolidated balance sheets of TSR, Inc. and subsidiaries as of May 31, 2009 and 2008 and the related consolidated statements of income, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (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 presentation of the financial statements. We believe that our audits provide a reasonable basis of our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of TSR, Inc. and subsidiaries as of May 31, 2009 and 2008, and their results of operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.



Jericho, New York
August 18, 2009

MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's shares of Common Stock trade on the NASDAQ Global Market under the symbol TSRI. The following are the high and low sales prices for each quarter during the fiscal years ended May 31, 2009 and 2008:

June 1, 2008 – May 31, 2009

	<u>1st</u> <u>Quarter</u>	<u>2nd</u> <u>Quarter</u>	<u>3rd</u> <u>Quarter</u>	<u>4th</u> <u>Quarter</u>
High Sales Price.....	3.84	3.00	2.37	1.92
Low Sales Price.....	2.35	1.78	1.55	1.56

June 1, 2007 – May 31, 2008

	<u>1st</u> <u>Quarter</u>	<u>2nd</u> <u>Quarter</u>	<u>3rd</u> <u>Quarter</u>	<u>4th</u> <u>Quarter</u>
High Sales Price	4.15	4.72	4.49	4.24
Low Sales Price	3.75	4.01	3.86	3.54

There were 115 holders of record of the Company's Common Stock as of July 31, 2009. Additionally, the Company estimates that there were approximately 1,500 beneficial holders as of that date. The Company paid a dividend of \$0.08 per quarter for fiscal 2008 and \$0.05 per quarter for the first two quarters of fiscal 2009. The Company has suspended payment of further dividends due to the continuing impact of the current economic environment. There can be no assurance that the Company will resume the payment of dividends.

DIRECTORS

Joseph F. Hughes

Chairman of the Board
Chief Executive Officer
President and Treasurer

Christopher Hughes

Senior Vice President and
President TSR Consulting
Services, Inc.

Robert A. Esernio

Director

James J. Hill

Director

John H. Hochuli, Jr.

Director

Raymond A. Roel

Director

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Chief Executive Officer
President and Treasurer

Christopher Hughes

Senior Vice President and
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John G. Sharkey

Vice President, Finance
and Secretary

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Copies of the Company's Form 10-K are available, without charge, to shareholders upon written request to:
John G. Sharkey, Vice President, Finance, TSR, Inc., 400 Oser Avenue, Hauppauge, NY 11788