



RECONDITIONED SYSTEMS, INC

ANNUAL REPORT 2018

Dear Fellow Shareholders,

I am very pleased to report that we were profitable this past year. Our margins have been severely impacted by the Arizona minimum wage increases. We have to increase our pay to workers to retain them as we have to pay higher wages to beginning workers and therefore higher pay to our existing workers.

For this fiscal year ending March 31, 2018, we made \$225 thousand on sales of \$10.86 million. This compares to a profit \$277 thousand on sales of \$10.15 million for the previous year ending March 31, 2017.

The US economy continues to grow at a very subdued rate. However, domestic business conditions remain good. Interest rates, while increasing, are still way below historic norms and inflation and energy costs remain low. We are in the tenth year of economic expansion, which is a record. I believe we are due for a recession this next year which of course will be negative for us. The tax cut to 21% will help us, but we first have to be profitable. Obviously fiscal 2019 will be very challenging for us. During this next year, we will be offering two new lines, which will help our margins going forward. This will be an investment we feel that we have to make. Meanwhile we are holding our other costs in line as best we can. We own our building which helps us to control our costs.

The Board of Directors decided not to pay an annual cash dividend this year. The board felt we should use the cash to fund the new lines mentioned above, which require a substantial investment. As in the past, any future dividends will depend on our performance and financial condition.

Although we are a non-reporting public company, I will continue to write a quarterly letter and post it on our Internet website at <http://www.rsisystems furniture.com>. Please keep track of our quarterly progress and filings by checking there under "About Us".

Scott W. Ryan  
Chairman of the Board

Reconditioned Systems, Inc.

Financial Statements

For the Years Ended  
March 31, 2018 and 2017

**RECONDITIONED SYSTEMS, INC.**  
**BALANCE SHEETS**  
**March 31, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$779,273	\$1,315,789
Accounts receivable	1,138,263	725,253
Prepaid Income Taxes	74,446	86,784
Deferred Income Taxes	14,000	41,400
Inventory	2,170,157	1,911,996
Prepaid expenses and other current assets	<u>56,794</u>	<u>36,857</u>
<b>Total current assets</b>	4,232,933	4,118,079
 <b>Property and Equipment, net:</b>	 4,635,322	 4,657,514
 <b>Other Assets:</b>		
Refundable deposits and other	<u>28,332</u>	<u>17,200</u>
 <b>Total Assets</b>	 <u>\$8,896,587</u>	 <u>\$8,792,793</u>
 <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities:</b>		
Accounts payable	\$703,106	\$558,660
Customer deposits	116,630	21,271
Accrued compensation and benefits	317,809	260,040
Income tax payable	193	320
Notes payable – current	<u>290,332</u>	<u>275,080</u>
<b>Total current liabilities</b>	<u>1,428,070</u>	<u>1,115,371</u>
 <b>Long-term Liabilities:</b>		
Notes payable – long term	1,585,164	1,887,303
Deferred Income Taxes	<u>98,400</u>	<u>134,300</u>
	<u>1,683,564</u>	<u>2,021,603</u>
 <b>Stockholders' Equity:</b>		
Common stock, no par value; 100,000,000 shares authorized, 1,734,652 shares issued, 960,878 and 960,878 shares outstanding, respectively	4,774,411	4,774,411
Retained earnings	<u>2,845,310</u>	<u>2,716,176</u>
	7,619,721	7,490,587
Less: treasury stock, 773,774 and 773,774 shares respectively, at cost	<u>(1,834,768)</u>	<u>(1,834,768)</u>
	<u>5,784,953</u>	<u>5,655,819</u>
 <b>Total Liabilities and Stockholders' Equity</b>	 <u>\$8,896,587</u>	 <u>\$8,792,793</u>

The Accompanying Notes are an Integral Part  
of the Financial Statements

**RECONDITIONED SYSTEMS, INC.**  
**STATEMENTS OF OPERATIONS**  
**For the Years Ended March 31, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
Sales	\$10,856,604	\$10,154,030
Cost of sales	<u>9,048,222</u>	<u>8,187,647</u>
Gross profit	1,808,382	1,966,383
Selling & administrative expenses	<u>1,433,058</u>	<u>1,415,311</u>
Income from operations	375,324	551,072
Other income (expense):		
Section 1256 gains (losses)	--	6,688
Interest income	434	964
Interest expense	(107,724)	(149,764)
Other	<u>6,736</u>	<u>189</u>
Net income before income taxes	274,770	409,149
Provision for income tax expense	<u>(49,548)</u>	<u>(131,794)</u>
Net income	<u>\$225,222</u>	<u>\$277,355</u>
Earnings per share : Basic and Diluted	<u>\$0.24</u>	<u>\$0.29</u>
Weighted average number of shares outstanding:		
Basic and Diluted	<u>960,878</u>	<u>960,922</u>

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**RECONDITIONED SYSTEMS, INC.**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
**For the Years Ended March 31, 2018 and 2017**

	Common Stock Shares	Common Stock Amount	Retained Earnings	Treasury Stock	Total
<b>Balance at March 31, 2016</b>	<b>960,978</b>	<b>\$4,774,411</b>	<b>\$2,679,067</b>	<b>\$(1,834,163)</b>	<b>\$5,619,315</b>
<b>Cash Dividend</b>			(240,246)		(240,246)
<b>Treasury stock purchases</b>	(100)			(605)	(605)
<b>Net income</b>			277,355		277,355
<b>Balance at March 31, 2017</b>	<b>960,878</b>	<b>\$4,774,411</b>	<b>\$2,716,176</b>	<b>\$(1,834,768)</b>	<b>\$5,655,819</b>
<b>Cash Dividend</b>			(96,088)		(96,088)
<b>Treasury stock purchases</b>					
<b>Net income</b>			225,222		225,222
<b>Balance at March 31, 2018</b>	<b>960,878</b>	<b>\$4,774,411</b>	<b>\$2,845,310</b>	<b>\$(1,834,768)</b>	<b>\$5,784,953</b>

The Accompanying Notes are an Integral Part  
of the Financial Statements

**RECONDITIONED SYSTEMS, INC.**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended March 31, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
Cash Flows from Operating Activities:		
Cash received from customers	\$10,462,934	\$10,595,834
Cash paid to suppliers and employees	(10,248,346)	(9,486,407)
Income taxes	(45,837)	(444,473)
Interest received and Section 1256	434	7,652
Interest paid	<u>(107,724)</u>	<u>(149,764)</u>
Net cash provided by operating activities	<u>61,461</u>	<u>522,842</u>
Cash Flows from Investing Activities:		
Purchase of property, equipment and amortizable assets	(215,002)	(146,166)
Other	<u>      -</u>	<u>5,000</u>
Net cash used by investing activities	<u>(215,002)</u>	<u>(141,166)</u>
Cash Flows from Financing Activities:		
Repayment of debt principal	(286,887)	(259,007)
Payment of cash dividend	(96,088)	(240,246)
Purchase of treasury stock	<u>      -</u>	<u>(605)</u>
Net cash used by financing activities	<u>(382,975)</u>	<u>(499,858)</u>
Decrease in cash and cash equivalents	(536,516)	(118,182)
Cash and cash equivalents at beginning of period	<u>1,315,789</u>	<u>1,433,971</u>
Cash and cash equivalents at end of period	<u>\$779,273</u>	<u>\$1,315,789</u>

The Accompanying Notes are an Integral Part  
of the Financial Statements

**RECONDITIONED SYSTEMS, INC.**  
**STATEMENTS OF CASH FLOWS (Continued)**  
**For the Years Ended March 31, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
Reconciliation of Net Income to Net Cash Provided by Operating Activities:		
Net Income	225,222	277,355
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	212,451	217,531
Provision for doubtful accounts	(12,604)	-
Changes in assets and liabilities:		
Accounts receivable	(400,406)	441,615
Inventory	(258,161)	117,340
Prepaid expenses and other assets	(6,331)	517
Current and Deferred income taxes	3,711	(312,679)
Accounts payable	144,446	27,435
Customer deposits	95,359	(23, 976)
Accrued compensation	<u>57,774</u>	<u>(222,296)</u>
Net cash provided by operating activities	<u>\$61,461</u>	<u>\$522,842</u>

The Accompanying Notes are an Integral Part  
of the Financial Statements

**RECONDITIONED SYSTEMS, INC.**  
**Notes to the Financial Statements**

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**Note 1.**

**Summary of Significant Accounting Policies, Nature of Operations, and Use of Estimates**

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**Nature of Business:**

Reconditioned Systems, Inc. (“RSI” or the “Company”), is a corporation that was incorporated in the State of Arizona in March 1987. The principal business purpose of the Company is the manufacturing and sale of office workstations comprised of panel systems to customers located throughout the United States and Canada. The Company markets its products primarily in the continental United States.

**Pervasiveness 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 revenues and expenses during the reporting periods. Actual results could differ from those estimates.

**Revenue Recognition:**

The Company recognizes a sale when its earnings process is complete. In connection with projects that are to be installed by a customer or an agent of the customer, the sale is recognized when the product is shipped to or possession is taken by the customer.

**Cash and Cash Equivalents:**

The Company considers all highly liquid debt instruments and money market funds purchased with an initial maturity of three (3) months or less to be cash equivalents.

**Accounts Receivable – Trade:**

Accounts receivable are reported at the customers’ outstanding balances less any allowance for doubtful accounts. The allowance is based upon a review of the individual accounts outstanding and the Company’s prior history of uncollectible receivables. Based on management’s assessment, the Company provides for estimated uncollectible amounts through a charge to earnings and a credit to a valuation allowance. Balances that remain outstanding after the Company has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. At March 31, 2018 and 2017, the Company has established an allowance for doubtful accounts in the amount of \$2,396 and \$15,000, respectively.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 1.**  
**Summary of Significant Accounting Policies, Nature of Operations, and Use of Estimates**  
**(Continued)**

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**Inventory:**

Inventory, which is primarily composed of used office workstations raw materials and manufacturing supplies, is stated at the lower of average cost or market. The Company reviews its inventory monthly and makes provisions for damaged and obsolete items. The Company contemplates its ability to alter the size of panels and other workstation components and designs projects so that the workstations are comprised of products currently in inventory in establishing its obsolescence reserve. At March 31, 2018 and 2017, the Company had established a reserve for damaged and obsolete inventory in the amount of \$0 and \$53,023, respectively.

**Property and Equipment:**

Property and equipment are recorded at cost. Major renewals and improvements are charged to the asset accounts while replacements, maintenance and repairs, which do not improve or extend the lives of respective assets, are expensed. At the time property and equipment are retired or otherwise disposed of, the assets and related depreciation accounts are relieved of applicable amounts. Gains or losses from retirements or sales are credited or charged to income. Depreciation is generally provided for on the straight-line basis over the following estimated useful lives of the assets:

	<u>Years</u>
Building & improvements	15-40
Office furniture and equipment	5 – 7
Machinery and equipment	5 – 7
Leasehold improvements	3 – 5
Vehicles	3 – 5
Showroom furniture	1 – 3

**Long-Lived Assets:**

The Company evaluates long-lived assets and certain identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. When undiscounted future cash flows are not expected to be sufficient to recover an asset's carrying amount, the asset is written down to its fair value.

Long-lived assets to be disposed of other than by sale are classified as held and used until they are disposed of. Long-lived assets to be disposed of by sale are classified as held for sale and are reported at the lower of carrying amount or fair value less cost to sell, and depreciation is ceased.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 1.**  
**Summary of Significant Accounting Policies, Nature of Operations, and Use of Estimates**  
**(Continued)**

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**Deferred Income Taxes:**

Deferred income taxes are provided on an asset and liability method, whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, there is uncertainty of using the operating losses in future periods. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

**Earnings Per Common and Common Equivalent Share:**

Basic earnings per share include no dilution and are computed by dividing income available to common stockholders by the weighted average number of shares outstanding for the period.

Diluted earnings per share amounts are computed based on the weighted average number of shares actually outstanding plus the shares that would be outstanding assuming the exercise of dilutive stock options, all of which are considered to be common stock equivalents. The number of shares that would be issued from the exercise of stock options has been reduced by the number of shares that could have been purchased from the proceeds at the average market price of the Company's stock. In addition, certain outstanding options are not included in the computation of diluted earnings per share because their effect would be antidilutive.

**Advertising:**

All direct advertising costs are expensed as incurred. The Company charged to operations \$5,597 and \$5,337 in advertising costs for the years ended March 31, 2018 and 2017, respectively.

**Shipping costs:**

Shipping costs include freight and mailing charges associated with delivery of goods from the company's warehouse to customer's designated locations. The company's policy is to classify shipping costs as part of cost of goods sold in the statement of operations.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 2.**  
**Concentrations**

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The Company maintains cash balances at various financial institutions. Deposits not to exceed \$250,000 at the financial institutions are insured by the Federal Deposit Insurance Corporation. As of March 31, 2018, the Company had approximately \$204,008 of uninsured cash.

In addition, the Company specializes in remanufacturing one particular original equipment manufacturers (OEM) line of office workstations. The business is dependent upon a readily available supply of new parts, as well as used product.

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**Note 3.**  
**Fair Value of Financial Instruments**

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The Company estimates that the fair value of all financial instruments at March 31, 2018 and 2017 does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying balance sheets. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. Considerable judgment is required in interpreting market data to develop the estimates of fair value, and accordingly, the estimates are not necessarily indicative of the amounts that the Company could realize in a current market exchange.

Estimated fair values of the Company's financial instruments (all of which are held for non-trading purposes), are as follows:

	March 31, 2018		March 31, 2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$779,273	\$779,273	\$1,315,789	\$1,315,789
Accounts receivable	\$1,138,263	\$1,138,263	\$725,253	\$725,253
Accounts payable	\$703,106	\$703,106	\$558,660	\$558,660
Notes payable	\$1,875,496	\$1,875,496	\$2,162,383	\$2,162,383

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 4.**  
**Property and Equipment**

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Property and equipment by major classifications are as follows:

	<u>March 31, 2018</u>	<u>March 31, 2017</u>
Land	\$1,547,830	\$1,547,830
Building & improvements	3,237,972	3,201,734
Office furniture and equipment	275,636	256,691
Machinery and equipment	1,013,820	910,120
Vehicles	<u>43,957</u>	<u>33,650</u>
	6,119,215	5,950,025
Accumulated depreciation	<u>(1,483,893)</u>	<u>(1,292,511)</u>
	<u>\$4,635,322</u>	<u>\$4,657,514</u>

Depreciation expense for the years ended March 31, 2018 and 2017 totaled \$191,381 and \$171,882 respectively.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 5.**  
**Pledged Assets and Line of Credit**

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As of March 31, 2018, the Company had a \$500,000 line of credit agreement with National Bank of Arizona. Under this agreement, interest is payable at the bank's Prime rate plus 1%. The line of credit is collateralized by accounts receivable, inventory, property and equipment, and intangibles, which total \$6,275,161. As of March 31, 2018, the Company had no outstanding borrowings on the line of credit and was in compliance with all of the covenants of the agreement. The line of credit matures on August 30, 2018.

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**Note 6.**  
**Notes Payable**

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On May 26, 2011, the Company closed escrow on the purchase of a 105,000 square foot commercial building located on an 8.62 acre parcel in Chandler, Arizona for a purchase price of \$4,375,000. The Company made a cash payment of \$1,000,000 and entered into a \$3,375,000 promissory note payable to the seller. Under the terms of the original promissory agreement, the Company was scheduled to make another payment of \$1,375,000 on September 1, 2013. The remaining principal balance of \$2,000,000 was to be amortized over ten years at a 6.5% interest rate, payable in monthly installments of \$22,709.59. On December 28, 2012, the Company terminated the original promissory agreement and entered into a revised note payable. Under the new promissory agreement, the Company made an additional cash payment of \$355,000 and entered into a \$3,000,000 promissory note payable to the seller to be amortized over ten years at a 6.5% interest rate, payable in monthly installments of \$34,064 beginning September 1, 2013. As a result of the modification in terms, the carrying value of the note was discounted by an additional \$20,000 for early payment. Effective September 1, 2017, the interest rate was reduced to 4.00% per annum, resulting in monthly payments of \$31,704.09 for 72 months.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 7.**  
**Operating Lease Commitments**

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The Company leases warehouse, and office space in Georgia. The lease agreement requires the Company to pay property taxes, insurance and maintenance costs.

Future minimum lease payments were as follows at March 31, 2018:

<u>March 31,</u>	<u>Amount</u>
2019	\$36,102
2020	<u>12,138</u>
	<u>\$48,240</u>

Rent expense under the operating lease agreement for the year ended March 31, 2018 was \$35,734

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**Note 8.**  
**Cash Dividends**

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On May 19, 2017, the Board of Directors approved a cash dividend of \$0.10 per share payable on August 31, 2017. Cash dividends paid totaled \$96,088 and was charged to retained earnings. On May 24, 2018, the Board of Directors elected to not pay a dividend.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 9.**  
**Income Taxes**

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The income tax expense is comprised of the following:

	For the Year Ended	
	<u>March 31, 2018</u>	<u>March 31, 2017</u>
Current Tax Expense:		
Federal	\$ 48,178	\$137,319
State	<u>9,870</u>	<u>23,175</u>
	<u>58,048</u>	<u>160,494</u>
Deferred Tax Expense:		
Federal	(12,200)	(16,700)
State	<u>3,700</u>	<u>(12,000)</u>
	<u>(8,500)</u>	<u>(28,700)</u>
Total Income Tax Expense	<u>\$49,548</u>	<u>\$131,794</u>

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 10.**  
**Income Taxes (Continued)**

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Significant components of the Company's deferred tax assets and liabilities are as follows:

	For the Year Ended	
	<u>March 31, 2018</u>	<u>March 31, 2017</u>
Deferred tax assets:		
Reserves, allowances and accruals	23,200	57,200
Deferred interest	<u>(9,200)</u>	<u>(15,800)</u>
Deferred tax asset	<u>\$14,000</u>	<u>\$41,400</u>
Deferred tax liability:		
Property and equipment related	\$76,650	\$87,300
Deferred interest	<u>21,750</u>	<u>47,000</u>
Deferred tax liability	<u>\$98,400</u>	<u>\$134,300</u>

Summary of valuation allowance:

Balance at April 1, 2017	\$ -
Addition for the year ended March 31, 2018	<u>-</u>
Balance at March 31, 2018	<u><u>-</u></u>

Realization of the net deferred tax assets is dependent on future reversals of existing taxable temporary differences and adequate future taxable income, exclusive of reversing temporary differences and carryforwards. Although realization is not assured, management believes that it is more likely than not that the net deferred tax assets will be realizable. The amount of the net deferred tax asset considered realizable could be reduced in the near term if actual future taxable income is lower than estimated, or if there are differences in the timing or amount of future reversals of existing taxable temporary differences.

**RECONDITIONED SYSTEMS, INC.**  
**Notes to Financial Statements (Continued)**

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**Note 11.**  
**Earnings Per Share**

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For the years ended March 31, 2018 and 2017 the following data shows amounts used in computing earnings per share and the effect on income and the weighted average number of shares of dilutive potential common stock.

	<b>March 31,</b>	
	<b><u>2017</u></b>	<b><u>2017</u></b>
<b>Basic and Diluted EPS</b>		
Income before extraordinary item	\$225,222	\$277,355
Extraordinary item	-	-
Net income	<u>\$225,222</u>	<u>\$277,355</u>
Weighted average number of shares outstanding	960,878	960,992
Effect of dilutive securities	<u>-</u>	<u>-</u>
Total common shares + assumed conversions	<u>960,878</u>	<u>960,922</u>
Basic and Diluted earnings per share	<u>\$0.24</u>	<u>\$0.29</u>

# Corporate Information

## COMMON STOCK LISTING AND TRADING

Reconditioned Systems, Inc. common stock is trading on the Pink Sheets under the ticker symbol RESY.

## CORPORATE HEADQUARTERS

Reconditioned Systems, Inc.  
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Chandler, Arizona 85226  
(480)968-1772  
(800)280-5000 Toll free  
(480)894-1907 Facsimile

## FOR INVESTOR RELATIONS

Visit our website at [www.rsisystemsurniture.com](http://www.rsisystemsurniture.com)

## Transfer Agent & Registrar

Zions First National Bank  
Corporate Trust  
1 South Main, 12<sup>th</sup> Floor  
Salt Lake City, UT 84113

## Officers and Directors

Scott W. Ryan  
Chairman

Dirk D. Anderson  
President, CEO & Director

David M. Ryan  
Director