



**Report of Wipfli LLP,
Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders
ARI Network Services, Inc.

We have audited the accompanying consolidated balance sheets of ARI Network Services, Inc. and Subsidiaries (the Company) as of July 31, 2008 and 2007 and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of July 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

Wipfli LLP
Milwaukee, Wisconsin
October 29, 2008



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Consolidated Financial Statements

ARI Network Services, Inc.
Years ended July 31, 2008 and 2007



ARI Network Services, Inc.
Consolidated Balance Sheets
(Dollars in Thousands, Except Per Share Data)

	<u>July 31</u>	
	<u>2008</u>	<u>2007</u>
Assets		
Current assets:		
Cash	\$ 1,086	\$ 1,050
Trade receivables, less allowance for doubtful accounts of \$178 and \$148 at July 31, 2008 and 2007, respectively	1,304	1,302
Work in process	264	223
Prepaid expenses and other	392	291
Deferred income taxes	330	555
Total current assets	<u>3,376</u>	<u>3,421</u>
Equipment and leasehold improvements:		
Computer equipment	5,647	5,324
Leasehold improvements	198	128
Furniture and equipment	2,842	2,749
	<u>8,687</u>	<u>8,201</u>
Less accumulated depreciation and amortization	7,523	6,991
Net equipment and leasehold improvements	<u>1,164</u>	<u>1,210</u>
Deferred income taxes	2,412	1,539
Goodwill	2,196	1,269
Other intangible assets	1,396	882
Other long term assets	53	-
Capitalized software product costs:		
Amounts capitalized for software product costs	13,209	12,455
Less accumulated amortization	11,613	10,849
Net capitalized software product costs	<u>1,596</u>	<u>1,606</u>
Total assets	<u>\$ 12,193</u>	<u>\$ 9,927</u>



	July 31	
	2008	2007
Liabilities and shareholders' equity		
Current liabilities:		
Current borrowings on line of credit	\$ 700	\$ —
Current portion of notes payable	676	1,023
Accounts payable	408	703
Deferred revenue	5,071	5,619
Accrued payroll and related liabilities	922	962
Accrued sales, use and income taxes	80	28
Accrued vendor specific liabilities	284	175
Other accrued liabilities	615	124
Current portion of capital lease obligations	95	8
Total current liabilities	8,851	8,642
Non-current liabilities:		
Notes payable (net of discount)	116	479
Long-term portion of accrued compensation	97	55
Other long-term liabilities	—	28
Capital lease obligations	233	5
Total non-current liabilities	446	567
Total liabilities	9,297	9,209
Shareholders' equity:		
Cumulative preferred stock, par value \$.001 per share, 1,000,000 shares authorized; 0 shares issued and outstanding at July 31, 2008 and 2007, respectively	—	—
Junior preferred stock, par value \$.001 per share, 100,000 shares authorized; 0 shares issued and outstanding at July 31, 2008 and 2007, respectively	—	—
Common stock, par value \$.001 per share, 25,000,000 shares authorized; 6,971,927 and 6,623,605 shares issued and outstanding at July 31, 2008 and 2007, respectively	7	7
Common stock warrants and options	501	195
Additional paid-in capital	95,148	94,627
Accumulated deficit	(92,708)	(94,091)
Other accumulated comprehensive loss	(52)	(20)
Total shareholders' equity	2,896	718
Total liabilities and shareholders' equity	\$ 12,193	\$ 9,927

See accompanying notes



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ARI Network Services, Inc.
Consolidated Statements of Income
(Dollars in Thousands, Except Per Share Data)

	Year ended July 31	
	2008	2007
Net revenues:		
Subscriptions, support and other services fees	\$ 11,909	\$ 11,290
Software licenses and renewals	2,115	2,187
Professional services	2,893	1,958
Total net revenues	16,917	15,435
Cost of products and services sold:		
Subscriptions, support and other services fees	1,010	1,188
Software licenses and renewals	814	956
Professional services	1,047	575
Total cost of products and services sold	2,871	2,719
Gross Margin	14,046	12,716
Operating expenses:		
Depreciation and amortization (exclusive of amortization of software products included in cost of products and services sold)	727	631
Customer operations and support	970	1,131
Selling, general and administrative	9,163	9,110
Software development and technical support	1,836	1,679
Restructuring	529	-
Net operating expenses	13,225	12,551
Operating income	821	165
Other income (expense):		
Interest expense	(99)	(153)
Other, net	71	93
Total other income (expense)	(28)	(60)
Income before provision for income taxes	793	105
Income tax benefit (expense)	590	(4)
Net income	\$ 1,383	\$ 101
Basic and diluted net income per common share:		
Basic	\$ 0.21	\$ 0.02
Diluted	\$ 0.20	\$ 0.02

See accompanying notes



ARI Network Services, Inc.
Consolidated Statements of Shareholders' Equity
(Dollars in Thousands)

	Number of Shares Issued and Outstanding		Par Value	
	Preferred Stock	Common Stock	Preferred Stock	Common Stock
Balance July 31, 2006	–	6,202,529	\$ –	\$ 6
Issuance of common stock under stock purchase plan	–	13,394	–	–
Issuance of common stock as contribution to 401(k) plan	–	18,556	–	–
Issuance of common stock from exercise of stock options	–	39,126	–	–
Issuance of common stock related to acquisitions	–	350,000	–	1
Stock based compensation	–	–	–	–
Net income	–	–	–	–
Foreign currency translation adjustments	–	–	–	–
Comprehensive income	–	–	–	–
Balance July 31, 2007	–	6,623,605	–	\$ 7
Issuance of common stock under stock purchase plan	–	5,541	–	–
Issuance of common stock as contribution to 401(k) plan	–	30,090	–	–
Return of common stock from 401(k) plan	–	(6,031)	–	–
Issuance of common stock under executive bonus plan	–	6,222	–	–
Issuance of common stock related to acquisitions	–	312,500	–	–
Stock based compensation	–	–	–	–
Net income	–	–	–	–
Foreign currency translation adjustments	–	–	–	–
Comprehensive income	–	–	–	–
Balance July 31, 2008	–	6,971,927	\$ –	\$ 7



Common Stock Warrants & Options	Paid in Capital	Accumulated Deficit	Other Accumulated Comprehensive Loss	Total
\$ 36	\$ 93,838	\$ (94,192)	\$ -	\$ (312)
-	23	-	-	23
-	41	-	-	41
-	19	-	-	19
-	706	-	-	707
159	-	-	-	159
-	-	101	-	101
-	-	-	(20)	(20)
-	-	-	-	81
\$ 195	\$ 94,627	\$ (94,091)	(20)	\$ 718
-	7	-	-	7
-	48	-	-	48
-	(10)	-	-	(10)
-	7	-	-	7
-	469	-	-	469
306	-	-	-	306
-	-	1,383	-	1,383
-	-	-	(32)	(32)
-	-	-	-	1,351
\$ 501	\$ 95,148	\$ (92,708)	\$ (52)	\$ 2,896

See accompanying notes



ARI Network Services, Inc.
Consolidated Statements of Cash Flows
(In Thousands)

	Year ended July 31	
	2008	2007
Operating activities		
Net income	\$ 1,383	\$ 101
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of software products	764	800
Amortization of deferred financing costs, debt discount and excess carrying value over face amount of notes payable	25	(15)
Depreciation and other amortization	727	631
Deferred income taxes	(648)	-
Stock based compensation related to stock options	306	159
Stock issued as contribution to 401(k) plan	38	41
Net change in assets and liabilities:		
Trade receivables, net	9	(318)
Work in process	(41)	(60)
Prepaid expenses and other	(91)	(36)
Other long term liabilities	(53)	-
Accounts payable	(364)	147
Deferred revenue	(571)	(16)
Accrued payroll related liabilities	9	(191)
Accrued sales, use and income taxes	52	(20)
Accrued vendor specific liabilities	109	71
Other accrued liabilities	373	(150)
Net cash provided by operating activities	2,027	1,144
Investing activities		
Purchase of equipment, software and leasehold improvements	(119)	(639)
Cash paid for goodwill and intangible assets related to acquisitions	(769)	(462)
Cash paid for other net assets related to acquisitions	(239)	(715)
Software product costs capitalized	(524)	(358)
Net cash used in investing activities	(1,651)	(2,174)
Financing activities		
Borrowings under line of credit	700	-
Payments under notes payable	(1,035)	(1,517)
Payments of capital lease obligations	(25)	(16)
Proceeds from issuance of common stock	7	42
Net cash used in financing activities	(353)	(1,491)
Effect of foreign currency exchange rate changes on cash	13	(13)
Net change in cash	36	(2,534)
Cash at beginning of period	1,050	3,584
Cash at end of period	\$ 1,086	\$ 1,050
Cash paid for interest	\$ 109	\$ 183
Cash paid for income taxes	\$ 5	\$ 18
Noncash investing and financing activities		
Capital lease obligations incurred for computer equipment	\$ 334	\$ -
Capital lease obligations acquired in connection with acquisitions	6	37
Accrued liabilities related to acquisitions	113	-
Debt issued in connection with acquisitions	300	1,060
Issuance of common stock related to payment of executive bonus	7	-
Issuance of common stock in connection with acquisitions	469	707

See accompanying notes



ARI Network Services, Inc. Notes to Consolidated Financial Statements

1. Description of Business and Significant Accounting Policies

Description of Business

ARI Network Services, Inc. (the "Company" or "ARI") is a leading provider of electronic parts catalogs, website solutions and related technology and services to increase sales, efficiency and customer satisfaction for dealers, distributors and manufacturers in various markets.

Manufacturers and distributors drive revenue and efficiency gains by leveraging ARI's dealer relationships and look to ARI as a partner to reach their dealers. Dealers rely on ARI's extensive network of manufacturer and distributor relationships and leverage this network into content and solutions which result in revenue and efficiency gains.

The Company provides robust Internet-based and CD-ROM interactive electronic parts catalogs of manufactured equipment to approximately 24,000 dealers in approximately 85 countries. It serves dealers in various market segments including outdoor power, power sports, appliance, agricultural, marine, recreation vehicles, floor maintenance, auto and construction. The Company also supplies eCommerce enabled websites, direct mail custom marketing and technology-related services.

ARI operates primarily in two business segments: the US and European operations. Each provides technology-enabled business solutions that connect manufacturers in selected industries with their service and distribution networks. Segmented operating information is provided to the Company's chief operating decision makers.

ARI's electronic parts catalogs, including its flagship PartSmart® product, dealer marketing services and eCommerce services, including its WebSiteSmart Pro™ product, enable partners in a service and distribution network to (a) conveniently reference parts, service bulletins and other technical reference information, (b) market to their customers and prospects and (c) exchange electronic business documents such as purchase orders, invoices, warranty claims and status inquiries. The Company briefly operated a business which offered financing and insurance services to dealers in the Powersports industry. This operation was closed in November 2007.

The electronic cataloging suite of products and services enable partners in a service and distribution network to look up electronically technical reference information such as illustrated parts lists, service bulletins, price files, repair instructions and other technical information regarding the products of multiple manufacturers.

The website suite of products and services allow dealers to establish quickly an online presence to reach beyond typical geographic constraints and extend their store hours,

allowing their customers to look up and order parts and accessories 24 hours a day, 7 days a week.

An important element of ARI's business is its relationship with over 85 dealer business management system providers through its COMPASS Partners™ program. A dealer business management system is used by a dealer to manage inventory, maintain accounting records, bill customers and focus marketing efforts. ARI software's ability to interface with these systems provides the dealer with a more robust, informative, and cost-effective solution.

ARI also provides eCommerce services to the North American agribusiness industry, accounting for 3% of fiscal 2008's total revenue.

No single customer accounted for 10% or more of ARI's revenue in fiscal 2008 or 2007.

Principles of Consolidation

The financial statements include the accounts of ARI Network Services, Inc. and its wholly owned subsidiaries, ARI Europe B.V. and ARI Outsourced F&I Center, LLC. All intercompany transactions and balances have been eliminated.

The functional currency of the Company's subsidiary in the Netherlands is the Euro; accordingly, monetary assets and liabilities are translated into United States dollars at the rate of exchange existing at the end of the period, and non-monetary assets and liabilities are translated into United States dollars at historical exchange rates. Income and expense amounts, except for those related to assets translated at historical rates, are translated at the weighted-average exchange rates during the period. Adjustments resulting from the re-measurement of the financial statements into the functional currency are charged or credited to comprehensive income (loss).

Cash and Cash Equivalents

For purposes of the statements 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.

The Company's investment policy, as approved by the Board of Directors, is designed to provide preservation of capital, adequate liquidity to meet projected cash requirements, optimum yields in relationship to risk, market conditions and tax considerations and minimum risk of principal loss through diversified short and medium term investments. Eligible investments include direct obligations of the U.S. Treasury, obligations issued or guaranteed by the U.S. government, certain time deposits, certificates of deposits issued by commercial banks, money market mutual funds, asset backed securities and municipal bonds. The Company's current investments include money market mutual funds with terms not exceeding ninety days.



Concentrations

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash deposits in bank accounts. Deposits in excess of amounts insured by the Federal Deposit Insurance Corporation (FDIC) of \$250,000 (\$100,000 as of July 31, 2008) are exposed to loss in the event of nonperformance by the institution. The Company had cash deposits in excess of the FDIC insurance coverage of \$986,000 and \$950,000 as of July 31, 2008 and 2007, respectively.

Trade Receivables and Credit Policy

Trade receivables are uncollateralized customer obligations due on normal trade terms, most of which require payment within 30 days from the invoice date. Payments of trade receivables are allocated to the specific invoices identified on the customer's remittance advice or, if unspecified, are applied to the earliest unpaid invoices.

The carrying amount of trade receivables is reduced by an allowance that reflects management's best estimate of the amounts that will not be collected. Management individually reviews all receivable balances that exceed 60 days from the invoice date and based on an assessment of current creditworthiness, estimates the portion, if any, of the balance that will not be collected. The allowance for potential credit losses is reflected as an offset to trade receivables in the accompanying balance sheets.

Work in Process

Work in process consists of billable professional services performed by the Company, for which revenue was recognized pursuant to contract accounting primarily using the percentage-of-completion method with progress-to-completion measured based upon labor hours incurred, which have not been invoiced as of the end of the reporting period.

Revenue Recognition

Revenue for use of the network and for information services is recognized on a straight-line basis over the period of the contract.

Revenue from annual or periodic maintenance fees is recognized ratably over the period the maintenance is provided. Revenue from catalog subscriptions is recognized on a straight-line basis over the subscription term.

Revenue from software licenses in multiple element arrangements is recognized ratably over the contractual term of the arrangement. The Company considers all arrangements with payment terms extending beyond 12 months not to be fixed or determinable and evaluates other arrangements with payment terms longer than normal to determine whether the arrangement is fixed or determinable. If the fee is not fixed or determinable, revenue is recognized as payments become due from the customer. Arrangements that include acceptance terms

beyond the Company's standard terms are not recognized until acceptance has occurred. If collectability is not considered probable, revenue is recognized when the fee is collected.

Arrangements that include professional services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. Types of services that are considered essential include customizing complex features and functionality in the products' base software code or developing complex interfaces within a customer's environment. When professional services are not considered essential, the revenue allocable to the professional services is recognized as the services are performed. When professional services are considered essential, revenue under the arrangement is recognized pursuant to contract accounting using the percentage-of-completion method with progress-to-completion measured based upon labor hours incurred. When the current estimates of total contract revenue and contract cost indicate a loss, a provision for the entire loss on the contract is made in the period the amount is determined.

Revenue on arrangements with customers who are not the ultimate users (resellers) is deferred if there is any uncertainty regarding the ability and intent of the reseller to sell such software independent of their payment to the Company.

Amounts invoiced to customers prior to recognition as revenue as discussed above are reflected in the accompanying balance sheets as deferred revenue.

Use of Estimates

The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The Company considers capitalization and amortization of software product costs, realizability and valuation of intangible assets, accruals for anticipated losses on projects and litigation, sales tax liabilities, various contract arrangements, and the deferred tax valuation allowance to be significant estimates that are subject to change in the near term.

Equipment and Leasehold Improvements

Equipment and leasehold improvements are stated at cost. Depreciation and amortization are computed under the straight-line method for financial reporting purposes and accelerated methods for income tax purposes. Depreciation and amortization have been provided over the estimated useful lives of the assets as follows:

	<u>Years</u>
Computer equipment	3-5
Leasehold improvements	7
Furniture and equipment	3-5



Leasehold improvements are amortized over the useful lives of the assets or the term of the related lease agreement, whichever is shorter.

Capitalized and Purchased Software Product Costs

Certain software development and acquisition costs are capitalized when incurred. Capitalization of these costs begins upon the establishment of technological feasibility. The establishment of technological feasibility and the ongoing assessment of recoverability of software costs require considerable judgment by management with respect to certain external factors, including, but not limited to, technological feasibility, anticipated future gross revenues, estimated economic life and changes in software and hardware technologies.

The annual amortization of software products is the greater of the amount computed using: (a) the ratio that current gross revenues for the network or a software product bear to the total of current and anticipated future gross revenues for the network or a software product, or (b) the straight-line method over the estimated economic life of the product which currently runs from three to five years. Amortization starts when the product is available for general release to customers. All other software development and support expenditures are charged to expense in the period incurred.

Impairment of Long-Lived Assets

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", equipment and leasehold improvements and capitalized software product costs are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected undiscounted cash flows is less than the carrying value of the related asset or group of assets, a loss is recognized for the difference between the fair value and carrying value of the asset or group of assets. Such analyses necessarily involve judgment. The Company evaluated the ongoing value of its long-lived assets as of July 31, 2008 and 2007. The Company incurred \$43,000 of impairment charges related to its PartSmart™ product, included in depreciation and amortization, in fiscal 2007 and none in fiscal 2008.

Deferred Financing Costs

Costs incurred to obtain long-term financing are included in other assets and are amortized over the term of the related debt.

Capitalized Interest Costs

In 2008 and 2007, interest costs of \$3,000 and \$6,000, respectively, were capitalized and included in the capitalized software product costs.

Insurance Premiums Receivable

The Company is the beneficiary of the total premiums it paid on a split-dollar life insurance policy at the death of the policy holder. Insurance premiums receivable are recorded at present value based on the average life expectancy of the policy holder and are included in other long term assets. Insurance premiums receivable at July 31, 2008 consisted of \$53,000, which is the present value of future life insurance premiums receivable of \$214,000 discounted at 8% over 18 years. There was no life insurance premiums receivable recorded prior to July 31, 2008.

Shipping and Handling

Revenue received from shipping and handling fees is reflected in net revenue. Costs incurred for shipping and handling are reported in cost of products and services sold.

Income Taxes

Income taxes are accounted for using an asset and liability approach, which requires the recognition of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in the financial statements or tax returns. The measurement of current and deferred tax assets and liabilities is based on provisions of enacted tax laws; the effects of potential future changes in tax laws or rates are not anticipated. If it is more likely than not that full realization of deferred income tax benefits is not expected, a deferred tax valuation allowance is recorded.

Foreign Currency Translation

The Company's Netherland subsidiary uses the euro as its functional currency. Accordingly, assets and liabilities are translated into U.S. dollars at year-end exchange rates, and revenues and expenses are translated at weighted-average exchange rates. The resulting translation adjustment is recorded as a separate component of shareholders' equity and will be included in the determination of net income (loss) only upon sale or liquidation of the subsidiary.

Stock-Based Compensation

On August 1, 2006, the Company adopted SFAS No. 123(R) (revised 2004) (SFAS No. 123(R)), "Share-Based Payment", to account for its stock option plans, which is a revision of SFAS No. 123 and SFAS No. 95 "Statement of Cash Flows". The Company adopted SFAS 123(R) using the modified prospective approach. Under this transition method, compensation cost recognized for the years ended July 31, 2008 and 2007 includes the cost for all stock options granted prior to, but not yet vested as of August 1, 2006. This cost was based on the grant-date fair value estimated in accordance with the original provisions of SFAS No. 123. The cost for all share-based awards granted subsequent to July 31, 2006, represents the grant-date fair value that was estimated in



accordance with the provisions of FAS No. 123(R). Results for prior periods have not been restated. Compensation cost for options will be recognized in earnings, net of estimated forfeitures, on a straight-line basis over the requisite service period. There were no capitalized stock-based compensation costs at July 31, 2008 and 2007.

Comprehensive Income (Loss)

Comprehensive income is a more inclusive financial reporting method that includes disclosure of financial information that historically has not been recognized in the calculation of net income. The Company has reported Comprehensive Income which includes net income and cumulative translation adjustments in the Consolidated Statements of Shareholders' Equity for the year ended July 31, 2008 and 2007.

Basic and Diluted Net Income Per Common Share

Basic net income per common share is computed by dividing net income by the basic weighted average number of common shares outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period and reflects the potential dilution that could occur if all of the Company's outstanding stock options and warrants that are in the money were exercised (calculated using the treasury stock method). The following table is a reconciliation of basic and diluted net income per common share for the periods indicated (in thousands, except per share data):

	<u>2008</u>	<u>2007</u>
Net income	\$ 1,383	\$ 101
Weighted-average common shares outstanding	6,678	6,378
Effect of dilutive stock options and warrants	225	172
Diluted weighted-average common shares outstanding	<u>6,903</u>	<u>6,550</u>
Net income per share:		
Basic	\$ 0.21	\$ 0.02
Diluted	\$ 0.20	\$ 0.02

Options that could potentially dilute net income per share in the future that are not included in the computation of diluted net income per share, as their impact is anti-dilutive

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Goodwill and Other Intangible Assets

Under Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets" goodwill and intangible assets deemed to have indefinite lives are not amortized, but are subject to annual impairment tests. Intangible assets with definitive lives at July 31, 2008 and 2007 consist primarily of costs of customer relationships, which are amortized over their estimated useful lives of five years. These assets were acquired in the Info Access acquisition on July 1, 2008 and

the OC-Net acquisition on January 26, 2007, where the fair values were determined using the discounted cash flow approach.

The Company performs annual impairment tests annually or more frequently if facts and circumstances warrant a review. The Company determined that there was a single reporting unit for the purpose of goodwill impairment tests under SFAS 142. For purposes of assessing the impairment of goodwill, the Company estimates the value of the reporting unit using the best evidence available, which in fiscal 2008 was a discounted cash flow model, consideration of recent transaction values and market capitalization. This fair value is then compared with the carrying value of the reporting unit. During fiscal 2008 and 2007 there were no impairments to goodwill.

Intangible assets with indefinite lives consisted of \$2,196,000 and \$1,269,000 of goodwill at July 31, 2008 and 2007, respectively.

Amortizable intangible assets costs consisted of the following (in thousands):

	<u>Customer Relationships</u>	<u>Accumulated Amortization</u>	<u>Net Amount</u>
Balance 7-31-07	\$ 1,000	\$ (119)	\$ 881
Additions	730	-	730
Amortization expense	-	(215)	(215)
Balance 7-31-08	<u>\$ 1,730</u>	<u>\$ (334)</u>	<u>\$ 1,396</u>

	<u>Finance Costs</u>	<u>Accumulated Amortization</u>	<u>Net Amount</u>
Balance 7-31-07	\$ 20	\$ (19)	\$ 1
Amortization expense	-	(1)	(1)
Balance 7-31-08	<u>\$ 20</u>	<u>\$ (20)</u>	<u>\$ -</u>

The estimated future amortization expense related to intangible assets for the years subsequent to July 31, 2008 is as follows (in thousands):

	<u>Year Ending July 31</u>
2009	\$ 383
2010	383
2011	383
2012	<u>247</u>
Total	<u>\$ 1,396</u>

During fiscal 2008 the Company reclassified \$190,000 from amortizable intangible assets to goodwill. The reclassification was related to the value assigned to workforce intangible assets acquired in the OC - Net acquisition during fiscal 2007. It was determined during fiscal 2008 that the nature of the workforce intangible assets capitalized required the assets to be presented with goodwill as required by Statement of Financial Accounting Standard 141 Business Combinations. The impact that this reclassification had on amortization expense was immaterial. The fiscal 2007 financial statements have been restated to conform to the fiscal 2008 presentation.



Accounting Pronouncements

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities — Including an amendment of FASB Statement No. 115." SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. SFAS No. 159 is effective for the Company August 1, 2008. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ("SFAS No. 157"). This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the Board having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The adoption of this guidance is not expected to have had a material impact on the Company's consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position (FSP) FAS 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP FAS 142-3"). FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, "Goodwill and Other Intangible Assets" FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008 and early adoption is prohibited.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" ("SFAS 161"). SFAS 161 requires companies with derivative instruments to disclose information that should enable financial statement users to understand how and why a company uses derivative instruments, how derivative instruments and related hedged items are accounted for under SFAS 133 and how derivative instruments and related hedged items affect a company's financial position, financial performance and cash flows. SFAS 161 is effective for the Company's fiscal year beginning August 1, 2009. The adoption of SFAS 161 is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51" ("SFAS 160"). SFAS 160 amends ARB No. 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a

subsidiary. It clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. It requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. SFAS 160 establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation. SFAS 160 is effective for the Company's fiscal year beginning August 1, 2009. The adoption of SFAS 160 is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141 (Revised 2007), "Business Combinations" ("SFAS 141(R)"). SFAS 141(R) retains the fundamental requirements of the original pronouncement requiring that the purchase method be used for all business combinations. SFAS 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination, establishes the acquisition date as the date that the acquirer achieves control and requires the acquirer to recognize the assets acquired, liabilities assumed and any noncontrolling interest at their fair values as of the acquisition date. In addition, SFAS 141(R) requires expensing of acquisition-related and restructure-related costs, remeasurement of earn out provisions at fair value, measurement of equity securities issued for purchase at the date of close of the transaction and non-expensing of in-process research and development related intangibles. SFAS 141(R) is effective for the Company's business combinations for which the acquisition date is on or after August 1, 2009.

2. Capitalized and Purchased Software Product Costs

The balance of capitalized and purchased software product costs consisted of the following (in thousands):

	Software		Net
	Product	Accumulated	Amortization
	Costs	Amortization	Amount
Balance 7-31-07	\$ 12,455	\$ (10,849)	\$ 1,606
Capitalized costs	524	-	524
Acquisitions	230	-	230
Amortization expense	-	(764)	(764)
Balance 7-31-08	<u>\$ 13,209</u>	<u>\$ (11,613)</u>	<u>\$ 1,596</u>

The estimated aggregate amortization expense for each of the five succeeding fiscal years related to capitalized and purchased software product costs subject to amortization expense consist of the following at July 31, 2008 (in thousands):

	Year Ending
	July 31
2009	\$ 684
2010	452
2011	277
2012	120
2013	<u>63</u>
Total	<u>\$ 1,596</u>



3. Notes Payable

Notes payable consist of the following at July 31 (in thousands):

	2008	2007
Notes payable	\$ 800	\$ 1,533
Less imputed interest	(8)	(33)
Less debt discount	-	(3)
Plus carrying value in excess of the face amount of the notes payable	-	5
	<u>792</u>	<u>1,502</u>
Less current maturities	676	1,023
Notes payable - non-current	<u>\$ 116</u>	<u>\$ 479</u>

On April 24, 2003, the Company restructured its debt. In exchange for previously outstanding securities, the Company issued to a group of investors (collectively, the "New Holders"), in aggregate, \$500,000 in cash, new unsecured notes in the amount of \$3.9 million (the "New Notes") and new warrants for 250,000 common shares, exercisable at \$1.00 per share (the "New Warrants"). The interest rate on the New Notes was prime plus 2%, adjusted quarterly. The New Notes were payable in \$200,000 quarterly installments commencing March 31, 2004 through December 31, 2005 and \$300,000 quarterly installments commencing March 31, 2006 at the prime interest rate plus 2%. The New Notes were paid in full on December 31, 2007.

In accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings," the exchange of the previously outstanding securities for \$500,000 in cash, the New Notes and the New Warrants was accounted for as a troubled debt restructuring and no gain was recorded. Instead the liability in excess of the future cash flows to the New Holders, which was approximately \$322,000, was amortized as a reduction of interest expense over the life of the New Notes.

On August 7, 2003, the Company purchased from WITECH Corporation 1,025,308 shares of the Company's common stock, 30,000 common stock warrants and 20,350 shares of Series A Preferred Stock for \$200,000 at closing and an \$800,000 promissory note which was payable in \$50,000 quarterly installments through September 30, 2007 at the prime interest rate plus 2%, adjusted quarterly. The note was paid in full on September 28, 2007.

The Company issued \$700,000 of notes and \$400,000 of future, non-interest bearing contingent payments in connection with the OC-Net acquisition in 2007. The interest rate on the notes is prime plus 2%, adjusted quarterly (effective rate of 7.00% as of July 31, 2008). The notes are payable in quarterly principal installments of \$58,333, commencing March 31, 2007 through December 31, 2009. The notes do not contain any financial covenants. The Company paid \$250,000 of the future contingent payments in February, 2008, and the remaining \$150,000, which includes \$8,000 of imputed interest, is due in January, 2009.

In 2008, the Company issued \$300,000 of notes payable in connection with the Info Access acquisition, of which \$100,000 is due on October 1, 2008 and \$200,000 is due on July 1, 2009. The interest rate on the payments is 6%.

Principal payments due on notes payable are as follows:

	Year Ending July 31
2009	\$ 676,000
2010	116,000
Total	<u>\$ 792,000</u>

4. Acquisitions

On January 26, 2007, the Company purchased all of the outstanding stock of OC-Net, Inc. ("OC-Net"), a privately held corporation in Cypress, CA, that provided website development and hosting services to the Power Sports market (which includes motorcycles, All Terrain Vehicles, snowmobiles and personal watercraft), as well as certain customers outside the Power Sports market. Consideration for the acquisition included approximately \$1.1 million in cash, 350,000 shares of the Company's common stock, \$700,000 in debt to the sellers and future contingent payments totaling up to \$400,000. It was determined that as of July 31, 2008 and 2007, it was more likely than not that the contingencies associated with the remaining \$150,000 would be resolved such that the Company would owe that amount. Accordingly, this amount has been recorded as a liability at July 31, 2008 and 2007.

The purchase price of this acquisition has been allocated to the following specific assets and liabilities acquired based on the fair value of those identified tangible and intangible assets and liabilities as determined by an independent valuation (in thousands):

Cash	\$ 41
Accounts receivable	99
Prepaid taxes	5
Equipment	101
Software	580
Goodwill	1,269
Other intangible assets	<u>1,000</u>
Total assets	<u>3,095</u>
Accounts payable	\$ 56
Deferred revenue	19
Capital leases	29
Deferred taxes	<u>7</u>
Total liabilities	<u>111</u>
Net assets acquired	<u>\$ 2,984</u>

Capitalized software is amortized over 4 years and intangibles related to customer relationships are amortized over 5 years. In connection with the acquisition, the Company entered into an employment agreement with Robert Hipp (the "Employment Agreement") to serve as a Marketing/Business Development Manager for the Company. The term of the Employment Agreement expires on January 26, 2009.



The following table shows the audited results of operations for the fiscal year ended July 31, 2008 and the unaudited pro forma results of operations for the fiscal year ended July 31, 2007, which assumes the acquisition of the OC-Net business occurred at the beginning of that period:

(in thousands, except per share data)

	2008	ProForma Results 2007
Revenue	\$ 16,917	\$ 16,094
Net income (loss)	1,383	(146)
Net income (loss)/share	\$ 0.21	\$ (0.02)
Net income (loss)/ diluted share	0.20	(0.02)

This pro forma information does not purport to be indicative of the results that actually would have been obtained if the combined operations had been conducted during the periods presented and is not intended to be a projection of future results.

On July 1, 2008, the Company acquired all of the assets related to electronic parts catalog (EPC), electronic commerce and certification testing for service technicians of Info Access, the micropublishing division of Eye Communications, Inc., of Hartland, Wis. Consideration for the acquisition included approximately \$1.0 million in cash, 312,500 shares of the Company's common stock, 125,000 of which is held in escrow based on contingent revenue retention and notes payable of \$300,000. It was determined that as of July 31, 2008, it was more likely than not that the contingencies associated with the shares in escrow would be resolved such that the Company would owe that amount. Accordingly, this amount has been recorded as outstanding stock at July 31, 2008.

The purchase price of this acquisition has been allocated to the following specific assets and liabilities acquired based on the fair value of those identified tangible and intangible assets and liabilities (in thousands):

Prepaid expenses	\$ 9
Software	230
Goodwill	927
Other intangible assets	730
Total assets	<u>1,896</u>
Deferred revenue	\$ 23
Capital leases	6
Total liabilities	<u>29</u>
Net assets acquired	<u>\$ 1,867</u>

Capitalized software is amortized over 2 years and intangibles related to customer relationships are amortized over 4 years.

5. Capital and Operating Leases

The Company leases office space and certain office equipment under operating lease arrangements expiring through 2012. The Company is generally liable for its share of increases in the landlord's direct operating expenses and real estate taxes related to the office space leases. Total rental expense for the operating leases was \$659,000 in 2008 and \$586,000 in 2007.

Where applicable, rent expense for leased offices is recognized on a straight-line basis over the lease terms, which differ from the pattern of payments required by the leases. Other accrued liabilities include \$18,000 of deferred rent at July 31, 2008 and \$48,000, of deferred rent at July 31, 2007. As more fully discussed in Note 12, the Company has a recorded liability totaling \$204,000 for estimated net future lease costs associated with closed offices.

The Company has certain capital lease agreements in place related to computer and office equipment. Minimum lease payments under remaining capital and operating leases are as follows (in thousands):

Fiscal year ending July 31	Capital Leases	Operating Leases
2009	\$ 128	\$ 563
2010	123	298
2011	111	230
2012	19	13
2013	16	-
Thereafter	-	-
Total minimum lease payments	<u>397</u>	<u>1,104</u>
Less amounts related to interest	69	-
Net minimum lease payments	<u>\$ 328</u>	<u>\$ 1,104</u>

6. Line of Credit

On July 9, 2004, the Company entered into a line of credit with JPMorgan Chase, N.A. which, as since amended, permits the Company to borrow an amount equal to 80% of the book value of all eligible accounts receivable plus 45% of the value of all eligible open renewal orders (provided the renewal rate is at least 85%) minus \$75,000, up to \$1,500,000, and bears interest at prime rate. Eligible accounts include certain non-foreign accounts receivable which are less than 90 days from the invoice date. The line of credit terminates July 9, 2009, and is secured by substantially all of the Company's assets. The line of credit limits repurchases of common stock, the payment of dividends, liens on assets and new indebtedness. As of July 31, 2008 and 2007, there was \$700,000 and \$-0-, respectively, outstanding on the line of credit.



7. Shareholders' Equity

Shareholder Rights Plan

On August 7, 2003, the Company adopted a Shareholder Rights Plan designed to protect the interests of common shareholders from an inadequate or unfair takeover, but not affect a takeover proposal which the Board of Directors believes is fair to all shareholders. Under the Shareholder Rights Plan adopted by the Board of Directors, all shareholders of record on August 18, 2003 received one Preferred Share Purchase Right for each share of common stock they owned. These Rights trade in tandem with the common stock until and unless they are triggered. Should a person or group acquire more than 10% of ARI's common stock (or if an existing holder of 10% or more of the common stock were to increase its position by more than 1%), the Rights would become exercisable for every shareholder except the acquirer that triggered the exercise. The Rights, if triggered, would give the rest of the shareholders the ability to purchase additional stock of ARI at a substantial discount. The rights will expire on August 18, 2013, and can be redeemed by the Company for \$0.01 per Right at any time prior to a person or group becoming a 10% shareholder.

8. Stock-based Compensation Plans

Total stock compensation expense recognized by the Company for the years ended July 31, 2008 and 2007 was approximately \$306,000 and \$159,000, respectively. As of July 31, 2008 and 2007, there was approximately \$481,000 and \$143,000, respectively, of total unrecognized compensation cost related to non-vested options granted under the plans.

The Company used the Black-Scholes model to value stock options granted. Expected volatility is based on historical volatility of the Company's stock. The expected life of options granted represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the contractual term of the options is based on the U.S. Treasury yields in effect at the time of grant. As stock-based compensation expense recognized in our results of operations is based on awards ultimately expected to vest, the amount has been reduced for estimated forfeitures. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on our historical experience. Prior to fiscal year 2007, we accounted for forfeitures as they occurred for the purposes of our pro forma information under SFAS 123.

The weighted average assumptions in the following table were used to estimate the fair value of options granted:

	Year ended July 31	
	2008	2007
Expected life (years)	10 years	10 years
Risk-free interest rate	4.5%	4.9%
Expected volatility	78.0%	122.0%
Expected forfeiture rate	20.9%	15.9%
Expected dividend yield	0.0%	0.0%

Employee Stock Purchase Plans

The Company's 2000 Employee Stock Purchase Plan has 175,000 shares of common stock reserved for issuance, and 154,322 of the shares have been issued as of July 31, 2008. All employees of the Company, other than executive officers, with nine months of service are eligible to participate. Shares may be purchased at the end of a specified period at the lower of 85% of the market value at the beginning or end of the specified period through accumulation of payroll deductions, not to exceed 5,000 shares per employee per year.

Stock Option Plans

On November 19, 2003, pursuant to its option exchange program, the Company accepted for cancellation from all stock option plans old options to purchase 319,186 shares of common stock, representing approximately 29% of the shares of common stock underlying all old options that were eligible for exchange in the offer. Subject to and in accordance with the terms of the offer, the Company issued, on the new option grant date, May 21, 2004, new options to purchase 245,944 shares of the Company's common stock from the 2000 Stock Option Plan in exchange for the old options cancelled in the offer. The new options were 50% vested immediately and of the remaining options, 25% vested on July 31, 2005 and 25% vested on July 31, 2006.

1991 Stock Option Plan

The Company's 1991 Stock Option Plan was terminated on August 14, 2001, except as to outstanding options. Options granted under the 1991 Plan may be either: (a) options intended to qualify as incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended (the Code), or (b) nonqualified stock options.



Any incentive stock option that was granted under the 1991 Plan could not be granted at a price less than the fair market value of the stock on the date of grant (or less than 110% of the fair market value in the case of holders of 10% or more of the voting stock of the Company). Nonqualified stock options were allowed to be granted at the exercise price established by the Compensation Committee, which could be less than, equal to or greater than the fair market value of the stock on the date of grant.

Each option granted under the 1991 Plan is exercisable for a period of ten years from the date of grant (five years in the case of a holder of more than 10% of the voting stock of the Company) or such shorter period as determined by the Compensation Committee and shall lapse upon the expiration of said period, or earlier upon termination of the participant's employment with the Company.

At its discretion, the Compensation Committee may require a participant to be employed by the Company for a designated number of years prior to exercising any options. The Committee may also require a participant to meet certain performance criteria, or that the Company meets certain targets or goals, prior to exercising any options.

Changes in option shares under the 1991 Plan are as follows:

	Year ended July 31, 2008			
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	125,686	\$ 2.31	1.89	\$ -
Granted	-	n/a	n/a	n/a
Exercised	-	n/a	n/a	n/a
Forfeited	(32,500)	\$ 2.28	n/a	n/a
Outstanding at end of period	93,186	\$ 2.27	1.23	\$ -
Exercisable at end of period	93,186	\$ 2.27	1.23	\$ -
	Year ended July 31, 2007			
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	146,686	\$ 2.28	2.85	\$ 13,125
Granted	-	n/a	n/a	n/a
Exercised	-	n/a	n/a	n/a
Forfeited	(21,000)	\$ 2.12	n/a	n/a
Outstanding at end of period	125,686	\$ 2.31	1.89	\$ -
Exercisable at end of period	125,686	\$ 2.31	1.89	\$ -

The range of exercise prices for options outstanding at July 31, 2008 and 2007 was \$2.06 to \$9.06.

1993 Director Stock Option Plan

The Company's 1993 Director Stock Option Plan ("Director Plan") has expired and is terminated except for outstanding options. The Director Plan originally had 150,000 shares of common stock reserved for issuance to non-employee directors. Options under the Director Plan were granted at the fair market value of the stock on the grant date.

Each option granted under the Director Plan is exercisable one year after the date of grant and cannot be exercised later than ten years from the date of grant.

Changes in option shares under the Director Plan are as follows:

	Year ended July 31, 2008			
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	1,313	\$ 2.65	2.97	\$ -
Granted	-	n/a	n/a	n/a
Exercised	-	n/a	n/a	n/a
Forfeited	-	n/a	n/a	n/a
Outstanding at end of period	1,313	\$ 2.65	1.97	\$ -
Exercisable at end of period	1,313	\$ 2.65	1.97	\$ -
	Year ended July 31, 2007			
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	1,313	\$ 2.65	3.97	\$ 152
Granted	-	n/a	n/a	n/a
Exercised	-	n/a	n/a	n/a
Forfeited	-	n/a	n/a	n/a
Outstanding at end of period	1,313	\$ 2.65	2.97	\$ -
Exercisable at end of period	1,313	\$ 2.65	2.97	\$ -

The range of exercise prices for options outstanding at July 31, 2008 and 2007 was \$2.00 to \$3.56.

2000 Stock Option Plan

The Company's 2000 Stock Option Plan ("2000 Plan") has 1,950,000 shares of common stock authorized for issuance. Options granted under the 2000 Plan may be



either: (a) options intended to qualify as incentive stock options under Section 422 of the Code, or (b) nonqualified stock options.

Any incentive stock option that is granted under the 2000 Plan may not be granted at a price less than the fair market value of the stock on the date of the grant (or less than 110% of the fair market value in the case of a participant who is a 10% shareholder of the Company within the meaning of Section 422 of the Code). Nonqualified stock options may be granted at the exercise price established by the Compensation Committee.

Each incentive stock option granted under the 2000 Plan is exercisable for a period of not more than ten years from the date of grant (five years in the case of a participant who is 10% shareholder of the Company). Nonqualified stock options do not have this restriction.

Eligible participants include current and prospective employees, non-employee directors, consultants or other persons who provide services to the Company and whose performance, in the judgment of the Compensation Committee or management of the Company, can have a significant effect on the success of the Company. Changes in option shares under the 2000 Plan are as follows:

Year ended July 31, 2008				
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	1,013,100	\$ 1.45	6.61	\$ 320,062
Granted	548,625	\$ 1.51	n/a	n/a
Exercised	-	n/a	n/a	n/a
Forfeited	(181,187)	1.18	n/a	n/a
Outstanding at end of period	1,380,538	\$ 1.51	7.36	\$ 150,967
Exercisable at end of period	937,203	\$ 1.48	6.28	\$ 150,967

Year ended July 31, 2007				
	Options	Wt-Avg Exercise Price	Wt-Avg Remaining Contractual Period	Aggregate Intrinsic Value
Outstanding at beginning of period	1,054,350	\$ 1.35	7.27	\$ 814,975
Granted	127,000	\$ 2.00	n/a	n/a
Exercised	(39,126)	\$ 0.52	n/a	n/a
Forfeited	(129,124)	\$ 1.46	n/a	n/a
Outstanding at end of period	1,013,100	\$ 1.45	6.61	\$ 320,062
Exercisable at end of period	875,425	\$ 1.39	6.29	\$ 310,823

The range of exercise prices for options outstanding at July 31, 2008 and 2007 was \$0.15 to \$2.74.

Changes in non-vested option shares under the 2000 Plan are as follows:

	Year ended July 31, 2008	
	Options	Wt-Avg Grant Date Fair Value
Non-vested at beginning of period	137,675	\$ 1.79
Granted	548,625	\$ 1.51
Vested	(226,249)	\$ 1.54
Forfeited	(16,716)	\$ 2.06
Non-vested at end of period	443,335	\$ 1.76

	Year ended July 31, 2007	
	Options	Wt-Avg Grant Date Fair Value
Non-vested at beginning of period	188,799	\$ 1.59
Granted	127,000	\$ 2.00
Vested	(49,000)	\$ 1.57
Forfeited	(129,124)	\$ 1.46
Non-vested at end of period	137,675	\$ 1.79

9. Income Taxes

The provision for income taxes is composed of the following (in thousands):

	Year ended July 31	
	2008	2007
Current:		
Federal	\$ 362	\$ 113
State	121	26
Utilization of net operating loss carryforwards	(425)	(135)
Deferred, net	(648)	-
	\$ (590)	\$ 4

Provision for income taxes is based on taxes payable under currently enacted tax laws and an analysis of temporary differences between the book and tax bases of our assets and liabilities, including various accruals, allowances, depreciation and amortization. The tax effect of these temporary differences and the estimated tax benefit from tax net operating losses are reported as deferred tax assets and liabilities in the balance sheet. An assessment of the likelihood that net deferred tax assets will be realized from future taxable income is performed. To the extent that management believes it is more likely than not that some portion, or all, of the deferred tax asset will not be realized, a valuation allowance is established. This assessment is based on all available evidence, both positive and negative, in evaluating the likelihood of realizability. Issues considered in the assessment include future reversals of



existing taxable temporary differences, estimates of future taxable income (exclusive of reversing temporary differences and carryforwards) and prudent tax planning strategies available in future periods. Because ultimately the realizability of deferred tax assets is highly subject to the outcome of future events, the amount established as valuation allowances is considered to be a significant estimate that is subject to change in the near term. To the extent a valuation allowance is established or there is a change in the allowance during a period, the change is reflected with a corresponding increase or decrease in the tax provision in the statement of operations.

The Company had a change in its estimated valuation allowance due to a historical trend of eight quarters of profit and projections of profit in the near future beginning in fiscal 2005. The Company continues to evaluate the realizability of deferred tax assets on a quarterly basis.

Significant components of the Company's deferred tax liabilities and assets as of July 31 are as follows (in thousands):

	2008	2007
Deferred tax assets:		
Net operating loss carryforwards	\$ 10,615	\$ 13,100
Alternative minimum tax credit carryforwards	78	66
Deferred revenue	1,832	2,065
Goodwill basis difference	430	514
Other	732	1,565
Total deferred tax assets	14,178	17,310
Valuation allowance for deferred tax assets	(10,618)	(14,176)
Net deferred tax asset	3,322	3,134
Deferred tax liabilities		
Software product costs and other	(580)	(660)
Intangibles	(288)	(380)
Net deferred taxes	\$ 2,742	\$ 2,094

As of July 31, 2008, the Company has unused net operating loss carryforwards for federal income tax purposes of \$27,402,000 expiring in 2009 through 2020.

A portion of these unused net operating loss carryforwards for federal income tax purposes totaling \$2,038,000 expire between 2012 and 2014 and are limited to \$116,000 annually that can be utilized to offset taxable income. Use of these net operating loss carryforwards is restricted under Section 382 of the Code because of changes in ownership in 1997.

In addition, the Company has net operating loss carryforwards for state income tax purposes totaling approximately \$21,648,000 expiring in 2009 through 2015.

A reconciliation between income tax expense and income taxes computed by applying the statutory federal income tax rate of 34% and the state rate of approximately 6% to income before income taxes is as follows (in thousands):

	2008	2007
Computed income taxes at 40%	\$ 296	\$ 42
Permanent items	4	8
Gross change in valuation allowance	(648)	-
Utilization of previously unrecognized benefit of net operating losses	(425)	(135)
Effective rate differences and other	183	89
Income tax expense (benefit)	\$ (590)	\$ 4

During 2008 and 2007, \$7,432,000 and \$7,642,000 respectively, of federal net operating loss carryforwards expired. These expired net operating loss carryforwards have been included in the calculation of the change in valuation allowance.

The Company adopted the provisions of Financial Accounting Standards Board, or FASB, Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48), on August 1, 2007. The implementation of FIN 48 did not have a significant impact on our results of operations or financial position and therefore no amounts were reserved for uncertain tax positions as of July 31, 2008.

10. Employee Benefit Plan

The Company has a qualified retirement savings plan (the 401(k) Plan) covering its employees. Each employee may elect to reduce his or her current compensation by up to 50%, up to a maximum of \$15,500 (\$20,500 over age 50) in calendar 2008 (subject to adjustment in future years to reflect cost of living increases) and have the amount of the reduction contributed to the 401(k) Plan. Company contributions to the 401(k) Plan are at the discretion of the Board of Directors. During 2008 and 2007, the Company issued 24,059 and 18,556 shares of common stock, respectively, as a discretionary contribution to the 401(k) Plan. The amounts charged to expense for the 401(k) contributions, net of forfeitures, were \$38,000 during 2008 and \$41,000 during 2007.

11. Changes in Accounting Estimates

During fiscal 2008, the Company had a change in its estimated valuation allowance related to deferred tax assets due to continual revisions and evaluations of the estimates of the expected results of operations for the next twelve months. The difference between the amounts previously recorded as a valuation allowance and the amount recorded was credited to income in fiscal 2008. The amount of this change in accounting estimate was approximately \$648,000. The impact of this change was to increase basic and diluted earnings per common share by \$0.09.



12. Restructuring

In July, the Company announced a restructuring that would consolidate its data conversion operations in Virginia into its Wisconsin location and consolidate the software development operations in Colorado into its California location. A charge was taken to reflect the following restructuring costs (in thousands):

Severance and related benefits	\$	292
Net future lease costs		204
Equipment disposition and other		33
Total restructuring costs	\$	<u>529</u>

13. Business Segments

Our business segments are internally organized primarily by geographic location of the operating facilities. In accordance with SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", we have segregated the Netherlands operation and the US operations into separate reportable segments. (Refer to Note 1, "Significant Accounting Policies", for a description of segment operations.) We evaluate the performance of and allocate resources to each of the segments based on their operating results excluding interest and taxes. The accounting policies for each of the segments are described in Note 1. Information concerning our operating business segments for fiscal 2008 and 2007 is as follows:

Business Segment Information (In thousands)

Revenue	2008	2007
Netherlands	\$ 763	\$ 668
United States	16,154	14,767
Consolidated	<u>\$ 16,917</u>	<u>\$ 15,435</u>
Net Income (Loss)	2008	2007
Netherlands	\$ (262)	\$ (800)
United States	1,645	901
Consolidated	<u>\$ 1,383</u>	<u>\$ 101</u>
Total Assets	2008	2007
Netherlands	\$ 1,306	\$ 1,061
United States	10,887	8,866
Consolidated	<u>\$ 12,193</u>	<u>\$ 9,927</u>

13. Concentration and Related Party

Briggs & Stratton Corporation ("Briggs") is one of the Company's customers and owns approximately 12% of the Company's stock. Briggs has entered into customer contracts with the Company and has provided vendor services to the Company in the ordinary course of business. Generally, the customer contracts are for one or two years and renew

annually thereafter unless either party elects otherwise. The Company invoiced Briggs approximately \$418,000 and \$498,000 for products and services provided during fiscal 2008 and fiscal 2007, respectively. Briggs had unpaid net trade receivables of \$212,000 or 17% and \$250,000 or 19% of total trade receivables outstanding as of July 31, 2008 and 2007, respectively, \$ -0- and \$1,000 of which was over 90 days at July 31, 2008 and July 31, 2007, respectively.

The vendor services provided by Briggs are for printing of materials which are generally resold to customers and included in cost of sales. Briggs invoiced the Company approximately \$156,000 and \$290,000 for printing services during fiscal 2008 and fiscal 2007, respectively, \$8,000 and \$9,000 of which were unpaid as of July 31, 2008 and 2007.

Gordon J. Bridge serves on the Company's board of directors. He was assigned by the board to help the Company evaluate potential strategic growth opportunities for the business for which he was compensated approximately \$108,000 and \$176,000 during fiscal 2008 and 2007, respectively.

14. Litigation

On June 23, 2008, Powersports Complete, LLC ("Powersports") filed a complaint in the United States District Court for the Eastern District of Wisconsin against the Company and its wholly-owned subsidiary, ARI Outsourced F&I Center, LLC ("ARI Outsourced"). The complaint claims, among other things, that the Company and ARI Outsourced owe \$56,960 to Powersports in connection with their business arrangements during 2007. The complaint also claims that Powersports, among other remedies, is entitled to compensatory damages in the amount of \$1,250,000 and punitive damages in the amount of \$2,500,000. The Company and ARI Outsourced filed their answer to the complaint on September 16, 2008. The answer denied that Powersports is entitled to the payments described above, and asserted numerous counterclaims against Powersports. There have not been any communication or settlement discussions among Powersports, ARI or ARI Outsourced since the answer was filed.