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TSR INC
Form 10-Q
April 03, 2007

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the period ended February 28, 2007

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission File Number: 0-8656

TSR, Inc.

(Exact name of registrant as specified in its charter)

Delaware

13-2635899

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

400 Oser Avenue, Hauppauge, NY 11788

(Address of principal executive offices)

631-231-0333

(Registrant's telephone number)

None

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the Registrant is large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer [] Accelerated filer [] Non-accelerated filer [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). [] Yes [X] No

SHARES OUTSTANDING

4,568,012 shares of common stock, par value \$.01 per share, as of March 31, 2007

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Part I. Financial Information
Item 1. Financial Statements

TSR, INC. AND SUBSIDIARIES

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CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS	February 28, 2007	May 31, 2006
	-----	-----
	(Unaudited)	
Current Assets:		
Cash and cash equivalents (Note 3)	\$ 2,109,166	\$ 2,660,739
Marketable securities (Note 5)	6,390,606	5,406,830
Accounts receivable (net of allowance for doubtful accounts of \$355,000)	8,208,416	8,272,963
Other receivables	95,932	90,172
Prepaid expenses	65,645	48,793
Prepaid and recoverable income taxes	79,271	320,156
Deferred income taxes	150,000	150,000
	-----	-----
Total current assets	17,099,036	16,949,653
Marketable securities (Note 5)	998,125	1,490,547
Equipment and leasehold improvements, at cost (net of accumulated depreciation and amortization of \$541,583 and \$544,946)	46,987	36,134
Other assets	49,653	49,653
Deferred income taxes	109,000	109,000
	-----	-----
	\$18,302,801	\$18,634,987
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts and other payables	\$ 286,503	\$ 209,840
Accrued expenses and other current liabilities	2,487,498	2,730,202
Advances from customers	1,541,443	1,538,985
Income taxes payable	--	102,974
	-----	-----
Total current liabilities	4,315,444	4,582,001
	-----	-----
Minority Interest	4,975	31,751
	-----	-----
Stockholders' Equity:		
Preferred stock, \$1 par value, authorized 1,000,000 shares; none issued	--	--
Common stock, \$.01 par value, authorized 25,000,000 shares; issued 6,228,326 shares	62,283	62,283
Additional paid-in capital	5,071,727	5,071,727
Retained earnings	20,879,673	20,918,526
	-----	-----
	26,013,683	26,052,536
Less: Treasury stock, 1,660,314 shares, at cost	12,031,301	12,031,301
	-----	-----
	13,982,382	14,021,235
	-----	-----
	\$18,302,801	\$18,634,987
	=====	=====

The accompanying notes are an integral part of these

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Condensed Consolidated Financial Statements.

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TSR, INC. AND SUBSIDIARIES
 CONSOLIDATED CONDENSED STATEMENTS OF EARNINGS
 FOR THE THREE AND NINE MONTHS ENDED FEBRUARY 28, 2007 AND 2006
 (UNAUDITED)

	Three Months Ended	
	February 28, 2007	February 28, 2006
Revenues, net	\$ 11,773,704	\$ 11,594,872
Cost of sales	9,722,403	9,486,969
Selling, general and administrative expenses	1,777,553	1,683,686
	11,499,956	11,170,655
Income from operations	273,748	424,217
Other income (expense):		
Interest and dividend income	118,965	93,644
Realized and unrealized gain (loss) from marketable securities, net	(1,228)	(4,864)
Minority interest in subsidiary operating profits .	(6,227)	(9,377)
Income before income taxes	385,258	503,620
Provision for income taxes	184,000	214,000
Net income	\$ 201,258	\$ 289,620
Basic and diluted net income per common share	\$ 0.04	\$ 0.06
Weighted average number of basic common shares outstanding	4,568,012	4,568,012
Weighted average number of diluted common shares outstanding	4,568,012	4,568,012

The accompanying notes are an integral part of these consolidated condensed financial statements.

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TSR, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE NINE MONTHS ENDED FEBRUARY 28, 2007 AND 2006
 (UNAUDITED)

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	Nine Months Ended February 28,	
	2007	2006
	-----	-----
Cash flows from operating activities:		
Net income	\$ 1,057,470	\$ 1,24
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	20,546	1
Realized and unrealized (gain) loss from marketable securities, net	(1,472)	
Minority interest in subsidiary operating profits	36,802	5
Deferred income tax benefit	--	6
Recovery of bad debt expense	--	(7
Changes in assets and liabilities:		
Accounts receivable - trade	64,547	(51
Other receivables	(5,760)	(
Prepaid expenses	(16,852)	
Prepaid and recoverable income taxes	240,885	(6
Other assets	--	
Accounts payable and accrued expenses	(166,041)	(46
Income taxes payable	(102,974)	1
Advances from customers	2,458	1
	-----	-----
Net cash provided by operating activities	1,129,609	30
	-----	-----
Cash flows from investing activities:		
Proceeds from maturities and sales of marketable securities	7,332,461	10,34
Purchases of marketable securities	(7,822,343)	(9,33
Purchases of fixed assets	(31,399)	(1
	-----	-----
Net cash (used in) provided by investing activities	(521,281)	99
	-----	-----
Cash flows from financing activities:		
Distributions to minority interest	(63,578)	(6
Cash dividends paid	(1,096,323)	(1,41
	-----	-----
Net cash used in financing activities	(1,159,901)	(1,47
	-----	-----
Net decrease in cash and cash equivalents	(551,573)	(18
Cash and cash equivalents at beginning of period	2,660,739	2,57
	-----	-----
Cash and cash equivalents at end of period	\$ 2,109,166	\$ 2,39
	=====	=====
Supplemental Disclosures:		
Income tax payments	\$ 576,000	\$ 91
	=====	=====

The accompanying notes are an integral part of these consolidated condensed financial statements.

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TSR, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FEBRUARY 28, 2007
(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying condensed consolidated interim financial statements include the accounts of TSR, Inc. and its subsidiaries (the "Company"). All significant inter-company balances and transactions have been eliminated in consolidation. These interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applying to interim financial information and with the instructions to Form 10-Q of Regulation S-X of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures required by accounting principles generally accepted in the United States of America and normally included in the Company's annual financial statements have been condensed or omitted. These interim financial statements as of and for the three and nine months ended February 28, 2007, are unaudited; however, in the opinion of management, such statements include all adjustments (consisting of normal recurring accruals) necessary to present fairly the consolidated financial position, results of operations, and cash flows of the Company for the periods presented. The results of operations for the interim periods presented are not necessarily indicative of the results that might be expected for future interim periods or for the full year ending May 31, 2007. These interim financial statements should be read in conjunction with the Company's consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended May 31, 2006.

2. 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. No options covering shares of common stock have been omitted from the calculations of diluted net income per common share for the three and nine month periods ended February 28, 2007 and 2006, respectively, because there are no options outstanding.

3 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 February 28, 2007:

Cash in banks	\$	--
Money Market Funds		2,109,166

		\$ 2,109,166

4. REVENUE RECOGNITION

The Company's contract computer programming services are generally provided under time and materials agreements with customers. Accordingly, the Company recognizes such revenues as services are provided. Advances from customers represent amounts received from customers prior to the Company's

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provision of the related services, credit balances from overpayments and certain escheat liabilities.

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 of Characterization of Reimbursements Received for 'Out-of-Pocket' Expenses Incurred."

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TSR, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
 FEBRUARY 28, 2007
 (UNAUDITED)

5. MARKETABLE SECURITIES

The Company accounts for its marketable securities in accordance with Statement of Financial Accounting Standards 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 are mostly less than one year), such securities have been classified as held-to-maturity and are carried at amortized cost. The Company's equity securities are classified as trading securities, which are carried at fair value with unrealized gains and losses included in earnings. The Company's marketable securities are summarized as follows:

	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Recorded Value
Current				
United States Treasury Securities	\$ 6,374,719	--	--	\$ 6,374,719
Equity Securities	16,866	--	(979)	15,887
	-----	-----	-----	-----
	\$ 6,391,585	\$ --	\$ (979)	\$ 6,390,606
	=====	=====	=====	=====
Long - Term				
United States Treasury Securities	\$ 998,125	\$ --	\$ --	\$ 998,125
	=====	=====	=====	=====

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TSR, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
 FEBRUARY 28, 2007
 (UNAUDITED)

6. STOCK OPTIONS

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The Company has one stock-based employee compensation plan in effect. Effective June 1, 2006, the Company accounts for all transactions under which employees receive shares of stock or other equity instruments in the Company in accordance with the revised provisions of SFAS No. 123, "Statement of Financial Accounting Standards No. 123 (FAS123 (R))," which requires that the fair market value of all share based payment transactions be recognized in the financial statements. This Statement 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 FAS123(R) at the beginning of fiscal 2007. The Company has not issued any share based payments as of February 28, 2007. The Company previously accounted for share-based employee compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees".

7. RECENT ACCOUNTING PRONOUNCEMENTS

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 - "Accounting for Uncertainty in Income Taxes" (FIN 48). This guidance is intended to provide increased consistency in the application of FASB Statement No. 109 - "Accounting for Income Taxes" by providing guidance with regard to the recognition and measurement of tax positions, and provide increased disclosure requirements. In particular, this interpretation requires uncertain tax positions to be recognized only if they are "more-likely-than-not" to be upheld based on their technical merits. Additionally, the measurement of the tax position will be based on the largest amount that is determined to have greater than a 50% likelihood of realization upon ultimate settlement. Any resulting cumulative effect of applying the provisions of FIN 48 upon adoption would be reported as an adjustment to the beginning balance of retained earnings (deficit) in the period of adoption. Management is in the process of evaluating the effects of this guidance which is effective for fiscal years beginning after December 15, 2006.

On September 15, 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. SFAS No. 157 provides guidance related to estimating fair value and requires expanded disclosures. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value. The standard does not expand the use of fair value in any new circumstances. The Company is evaluating SFAS No. 157 and its impact on the Company's consolidated financial statements.

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TSR, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED
FEBRUARY 28, 2007
(UNAUDITED)

8. DIVIDENDS

On March 30, 2007 the Board of Directors of the Company declared that a regular quarterly cash dividend of \$0.08 per share for the quarter ended February 28, 2007 would be paid on May 1, 2007 to shareholders of record as of April 16, 2007. This dividend will amount to approximately \$365,000 and

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will be paid from the Company's cash and marketable securities.

9. MAJOR CUSTOMER

In June 2006, the New York State Office of General Services, Procurement Services Group ("OGS") terminated its contract with the Company. The OGS actions were due to the report of an investigation by the Office of the Special Commissioner of Investigation of the New York City Department of Education ("DOE"). The investigative report concluded that the Company operated improperly from 2001 through the spring of 2003 by using a subcontracting arrangement to obtain programmers for positions with the DOE. The subcontracting was with a small firm that was owned by an individual who worked as a consultant under contract at the DOE in a supervising capacity and sometimes was involved in decisions to select consultants that financially benefited both him and the Company. The investigative report also suggested that the Company received advanced information as to new positions from this individual and that the subcontracting increased the costs to the DOE since two firms, instead of one, profited from this arrangement.

All new placements with the DOE, including renewals of existing placements, were being made under this OGS contract prior to its termination. As a result, until a new OGS contract is entered into, the Company will not be able to make new placements or renew existing placements with the DOE. The termination does not affect existing placements with the DOE until the date such positions are scheduled to expire. At May 31, 2006 the Company had forty-one consultants placed with the DOE. As a result of the termination, consultants placed with the DOE who came up for renewal have not been renewed.

DOE also asserted a claim against the Company for a reimbursement due to the Company's subcontracting without written authorization. On August 29, 2006, the DOE and the Company agreed in principle to resolve these claims and permit the Company to be treated as a "responsible vendor" upon making a payment to DOE and appointment of an independent compliance monitor to monitor the Company's compliance with the DOE agreement. Due to the claim asserted by DOE and the proposed settlement, the Company established a reserve of \$900,000 as of May 31, 2006. While the Company believes that its subcontracting did not result in overcharges to DOE, it has agreed to settle the matter in order to avoid the expense and uncertainty of litigation. In addition to the settlement of the claim, the Company and the DOE were also negotiating an agreement which would have enabled the Company to continue placing new consultants with the DOE, which included, among other things, a monitoring agreement. The Company and the DOE have not been able to finalize the terms of this agreement. The Company does not expect the failure to reach this agreement to affect the agreement in principle to settle the DOE claim. As a result, the DOE has advised the Company that the 11 remaining consultants will be terminated in the near future.

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PART I. FINANCIAL INFORMATION

ITEM 2.

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

The following discussion and analysis should be read in conjunction with the

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Condensed Consolidated Financial Statements and the notes to such financial statements.

Forward-Looking Statements

Certain statements contained in Management's Discussion and Analysis of Financial Condition and Results of Operations, 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: 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; the 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 settlement with the NYC Department of Education (DOE) and the Company's ability to continue to provide consultants to the DOE; the impact on the Company's business due to the merger of AT&T and SBC Communications, Inc.; the impact of changes in the industry, such as the use of vendor management companies in connection with the consulting 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.

Results of Operations

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

Three months ended February 28, 2007 compared with three months ended February

28, 2006

	(Dollar amounts in Thousands)			
	Three Months Ended			
	February 28,			
	2007		2006	
	-----		-----	
	Amount	% of	Amount	% of
		Revenues		Revenues
Revenues	\$11,774	100.0	\$11,595	100.0
Cost of sales	9,722	82.6	9,487	81.8
	-----		-----	
Gross profit	2,052	17.4	2,108	18.2
Selling, general, and administrative expenses	1,778	15.1	1,684	14.5
	-----		-----	
Income from operations	274	2.3	424	3.7
Other income	111	1.0	80	0.6
	-----		-----	

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Income before income taxes	385	3.3	504	4.3
Provision for income taxes	184	1.6	214	1.8
	-----	-----	-----	-----
Net income	\$ 201	1.7	\$ 290	2.5
	=====	=====	=====	=====

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TSR, INC. AND SUBSIDIARIES

REVENUES

Revenues consist primarily of revenues from computer programming consulting services. Revenues for the quarter ended February 28, 2007 increased \$179,000 or 1.5% from the comparable period in fiscal 2006. Due to the contract suspension with the NYC Department of Education (DOE), the consultants on billing with DOE decreased from 41 at May 31, 2006 to 11 at the end of the current quarter. Despite this reduction in the number of consultants on billing at DOE, the overall average number of consultants on billing only decreased from 342 in the prior year quarter to 326 for the current quarter. Additional placements at other accounts, many at higher billing rates, have offset much of the reduction at DOE and, therefore, revenues have increased. After the end of the quarter, as described in Footnote 9 to the Condensed Consolidated Financial Statements, the DOE has advised the Company that the 11 remaining consultants will be terminated in the near future.

As a result of the merger of AT&T with SBC Communications, Inc., Procurestaff, which had been the vendor management company for AT&T is currently one of many vendors to the new AT&T and no longer serves as the primary vendor manager. Due to these changes, the Company experienced a decrease in new placements with AT&T beginning in the second fiscal quarter. This has reduced the number of consultants on billing with AT&T from 90 at November 30, 2006 to 79 at February 28, 2007. The Company is unable to predict whether this change of relationship will continue to impact the Company's business relationship with AT&T.

COST OF SALES

Cost of sales for the quarter ended February 28, 2007, increased \$235,000 or 2.5% to \$9,722,000 from \$9,487,000 in the prior year period. Cost of sales as a percentage of revenues increased from 81.8% in the quarter ended February 28, 2006 to 82.6% in the quarter ended February 28, 2007. The increase in cost of sales as a percentage of revenues was primarily attributable to discount programs instituted or expanded by customers. These discount programs decrease revenues without allowing offsetting cost reductions.

Cost of sales as a percentage of revenues increased, in part, because of a decline in revenues at AT&T, the Company's largest customer, due to Procurestaff offering further discounts to AT&T to maintain its relationship. This required the Company to reduce what it received from Procurestaff, which further reduced the Company's margins on its AT&T business.

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 increased \$94,000 or 5.6% from \$1,684,000 in the quarter ended February 28, 2006 to \$1,778,000 in the quarter ended February 28, 2007. This increase was primarily attributable to an increase in the number of technical recruiters and sales executives. Additional personnel have been hired to address increasing competition. The Company expects to

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continue to hire additional experienced sales executives and technical recruiters.

INCOME FROM OPERATIONS

In spite of the increase in revenues, income from operations decreased \$150,000 or 35.4% from \$424,000 in the quarter ended February 28, 2006 to \$274,000 in the quarter ended February 28, 2007. The discount programs which have caused an increase in cost of sales as a percentage of revenues, along with the expenses related to the hiring of additional sales and recruiting personnel, have reduced income from operations.

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TSR, INC. AND SUBSIDIARIES

OTHER INCOME

Other income resulted primarily from interest and dividend income, which increased by \$25,000 to \$119,000 due to higher interest rates in the quarter ended February 28, 2007. Additionally, the Company had an unrealized loss of \$1,000 in the quarter ended February 28, 2007 versus a net unrealized loss of \$5,000 in the quarter ended February 28, 2006 from marketable securities due to market adjustments of its trading securities equity portfolio.

INCOME TAXES

The effective income tax rate of 47.8% for the quarter ended February 28, 2007 increased from a rate of 42.5% in the quarter ended February 28, 2006 due to an adjustment to the reversal of prior years' income tax over accruals taken in the first two quarters of fiscal 2007.

Nine months ended February 28, 2007 compared with nine months ended February 28, 2006

	(Dollar amounts in Thousands)			
	Nine Months Ended February 28, 2007		2006	
	% of Amount	Revenues	% of Amount	Revenues
Revenues	\$36,775	100.0	\$35,889	100.0
Cost of sales	29,978	81.5	28,886	80.5
Gross profit	6,797	18.5	7,003	19.5
Selling, general, and administrative expenses	5,331	14.5	5,026	14.0
Income from operations	1,466	4.0	1,977	5.5
Other income	311	0.8	193	0.5
Income before income taxes	1,777	4.8	2,170	6.0
Provision for income taxes	720	1.9	923	2.5

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	-----	-----	-----	-----
Net income	\$ 1,057	2.9	\$ 1,247	3.5
	=====	=====	=====	=====

REVENUES

Revenues consist primarily of revenues from computer programming consulting services. Revenues for the nine months ended February 28, 2007 increased \$886,000 or 2.5% from the comparable period in fiscal 2006. Due to the contract suspension with the NYC Department of Education (DOE), the consultants on billing with DOE decreased from 41 at May 31, 2006 to 11 at the end of the current period. Despite this reduction in the number of consultants on billing at DOE, the overall average number of consultants on billing only decreased from 345 in the prior year period to 339 for the current period. Additional placements at other accounts, many at higher billing rates, have offset most of the reduction at DOE and, therefore, revenues have increased. After the end of the quarter, as described in Footnote 9 to the Condensed Consolidated Financial Statements, the DOE has advised the Company that the 11 remaining consultants will be terminated in the near future.

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COST OF SALES

Cost of sales for the nine months ended February 28, 2007, increased \$1,092,000 or 3.8% to \$29,978,000 from \$28,886,000 in the prior year period. Cost of sales as a percentage of revenues increased from 80.5% in the nine months ended February 28, 2006 to 81.5% in the nine months ended February 28, 2007. The increase in cost of sales as a percentage of revenues was primarily attributable to discount programs instituted or expanded by customers. These discount programs decrease revenues without allowing offsetting cost reductions.

Cost of sales as a percentage of revenues increased in part, because of a decline in revenues at AT&T, the Company's largest customer, due to Procurestaff offering further discounts to AT&T to maintain its relationship. This required the Company to reduce what it received from Procurestaff, which further reduced the Company's margins on its AT&T business.

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 increased \$305,000 or 6.1% from \$5,026,000 in the nine months ended February 28, 2006 to \$5,331,000 in the nine months ended February 28, 2007. This increase was primarily attributable to an increase in the number of technical recruiters and sales executives. Additional personnel have been hired to address increasing competition. The Company expects to continue to hire additional sales executives and technical recruiters.

INCOME FROM OPERATIONS

In spite of the increase in revenues, income from operations decreased \$511,000 or 25.8% from \$1,977,000 in the nine months ended February 28, 2006 to \$1,466,000 in the nine months ended February 28, 2007. The discount programs which have caused an increase in cost of sales as a percentage of revenues, along with the expenses related to the hiring of additional sales and recruiting personnel, have reduced income from operations.

OTHER INCOME

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Other income resulted primarily from interest and dividend income, which increased by \$91,000 to \$346,000 due to higher interest rates in the nine months ended February 28, 2007. Additionally, the Company had an unrealized gain of \$1,000 in the nine months ended February 28, 2007 versus a net unrealized loss of \$5,000 in the nine months ended February 28, 2006 from marketable securities due to market adjustments of its trading securities equity portfolio.

INCOME TAXES

The effective income tax rate of 40.5% for the nine months ended February 28, 2007 decreased from a rate of 42.5% in the nine months ended February 28, 2006 due to lower state and local taxes and reversal of prior years' income tax over accruals.

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TSR, INC. AND SUBSIDIARIES

LIQUIDITY AND CAPITAL RESOURCES

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

At February 28, 2007, the Company had working capital of \$12,784,000 and cash and cash equivalents of \$2,109,000 as compared to working capital of \$12,368,000 and cash and cash equivalents of \$2,661,000 at May 31, 2006. The Company's working capital also included \$6,391,000 and \$5,407,000 of marketable securities with maturities of less than one year at February 28, 2007 and May 31, 2006, respectively. The working capital and marketable securities increased primarily due to the reclassification of a security from long-term to current.

Net cash provided by operating activities of \$1,130,000 for the nine months ended February 28, 2007, compared to \$300,000 of cash provided for the nine months ended February 28, 2006. The cash provided by operating activities in the nine months ended February 28, 2007 resulted primarily from the Company's net income. In the nine months ended February 28, 2006 an increase in accounts receivable and a decrease in accrued expenses significantly reduced the cash flow provided by the Company's net income.

Net cash used in investing activities of \$521,000 for the nine months ended February 28, 2007 primarily resulted from purchasing US Treasury Securities in excess of maturities. Net cash provided by investment activities of \$996,000 for the nine months ended February 28, 2006 primarily resulted from maturities of US Treasury Securities in excess of purchases.

Net cash used in financing activities of \$1,160,000 and \$1,477,000 for the nine month periods ended February 28, 2007 and 2006, respectively, resulted primarily from cash dividends.

The Company's capital resource commitments at February 28, 2007 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.

The Company's cash and marketable securities were sufficient to enable it to meet its cash requirements during the nine months ended February 28, 2007. The Company has available a revolving line of credit of \$5,000,000 with a major money center bank through October 6, 2007. As of February 28, 2007, no amounts were outstanding under this line of credit.

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TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

Contractual Obligations -----	PAYMENTS DUE BY PERIOD			
	TOTAL -----	LESS THAN 1 YEAR -----	1-3 YEARS -----	3-5 YEARS -----
Long-Term Debt	--	--	--	--
Capital Lease Obligations	--	--	--	--
Operating Leases	533,000	256,000	219,000	58,000
Purchase Obligations	--	--	--	--
Consulting Contract	50,000	50,000	--	--
Other Long-Term Liabilities Reflected on the Registrant's Balance Sheet under GAAP	--	--	--	--
	-----	-----	-----	-----
Total	\$583,000	\$306,000	\$219,000	\$58,000
	=====	=====	=====	=====

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TSR, INC. AND SUBSIDIARIES

RECENT ACCOUNT PRONOUNCEMENTS

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 - "Accounting for Uncertainty in Income Taxes" (FIN 48). This guidance is intended to provide increased consistency in the application of FASB Statement No. 109 - "Accounting for Income Taxes" by providing guidance with regard to the recognition and measurement of tax positions, and provide increased disclosure requirements. In particular, this interpretation requires uncertain tax positions to be recognized only if they are "more-likely-than-not" to be upheld based on their technical merits. Additionally, the measurement of the tax position will be based on the largest amount that is determined to have greater than a 50% likelihood of realization upon ultimate settlement. Any resulting cumulative effect of applying the provisions of FIN 48 upon adoption would be reported as an adjustment to the beginning balance of retained earnings (deficit) in the period of adoption. Management is in the process of evaluating the effects of this guidance which is effective for fiscal years beginning after December 15, 2006.

On September 15, 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. SFAS No. 157 provides guidance related to estimating fair value and requires expanded disclosures. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value. The standard does not expand the use of fair value in any new circumstances. The Company is evaluating SFAS No. 157 and its impact on the Company's consolidated financial statements.

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TSR, INC. AND SUBSIDIARIES

CRITICAL ACCOUNTING POLICIES

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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 the Company's consolidated financial statements, contained in its May 31, 2006 Annual Report on Form 10-K, as filed with the SEC. The Company believes that those accounting policies require the application of management's most difficult, subjective or complex judgments. There have been no changes in the Company's significant accounting policies as of February 28, 2007.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company's earnings and cash flows are subject to fluctuations due to (i) changes in interest rates primarily affecting its income from the investment of available cash balances in money market funds and (ii) changes in market values of its investments in trading equity securities. Under its current policies, the Company does not use interest rate derivative instruments to manage exposure to interest rate changes. The Company's present exposure to changes in the market value of its investments in equity securities is not significant.

ITEM 4. CONTROLS AND PROCEDURES

DISCLOSURE CONTROLS AND PROCEDURES. The Company conducted an evaluation, under the supervision and with the participation of the principal executive officer and principal financial officer, of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based on this evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective.

INTERNAL CONTROL OVER FINANCIAL REPORTING. There was no change in the Company's internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) during the Company's most recently reported completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1A. RISK FACTORS

There are no material changes to the risk factors described in the Form 10-K, filed on September 12, 2006, except as follows:

DEPENDENCE ON SIGNIFICANT CUSTOMERS

As described under Part I, Item 2, the Company's relationship with AT&T has changed due to the merger of AT&T with SBC Communications and the resulting change in the relationship with AT&T of Procurestaff, through which the Company contracts with AT&T. This change has had a further impact on the Company's profit margins on consultants placed with AT&T and recently created a decrease in new placements with AT&T. The Company cannot predict the extent to which this change will adversely affect the number of consultants placed with AT&T.

