

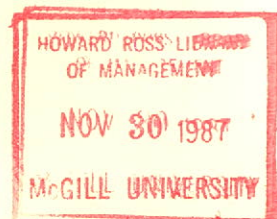






Systemhouse delivers integrated  
information systems for  
commercial and government  
customers.

Systemhouse gratefully acknowledges  
the cooperation of our customers who appear  
in this report.





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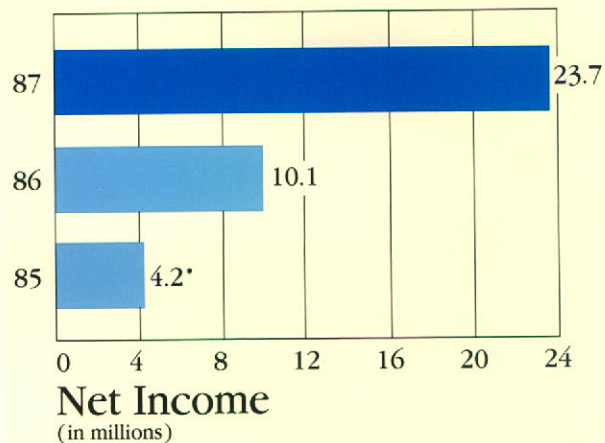
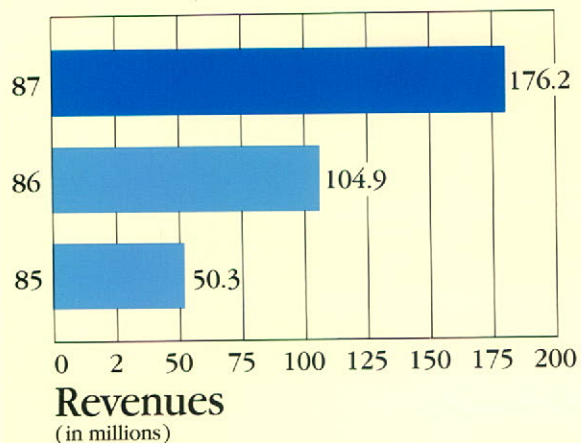
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All financial information in this annual report is expressed in Canadian dollars unless otherwise stated.

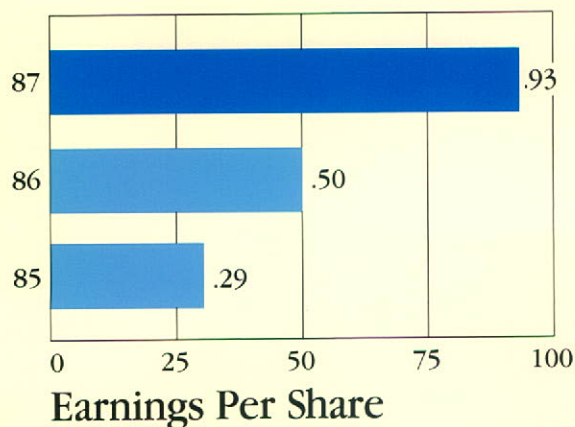


# Financial Highlights

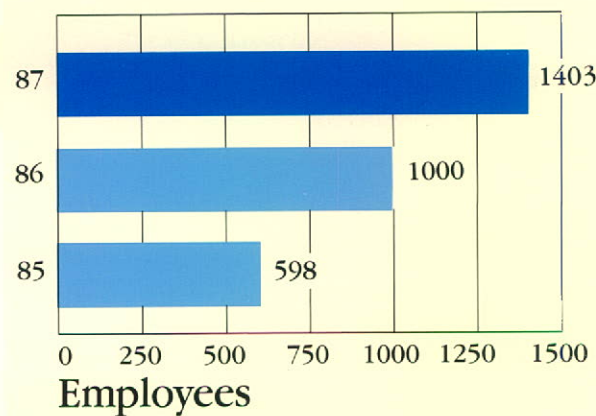
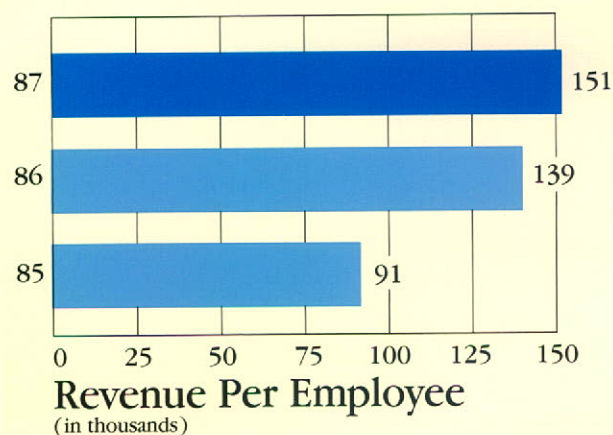
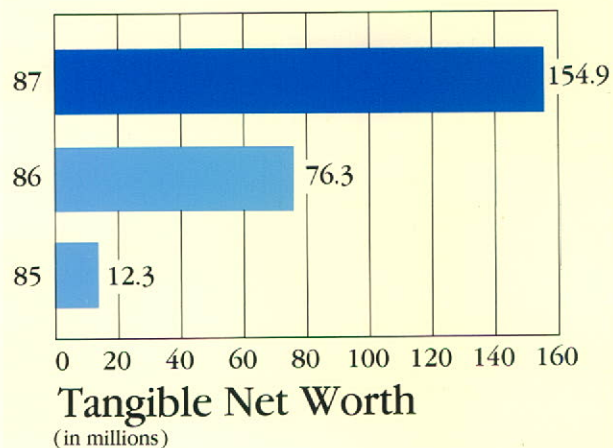
From Continuing Operations



\*Excludes gain of \$4.8 million from sale of discontinued operations



All years include effect of 2 for 1 stock split in December 1986



# Message to Shareholders

Systemhouse enjoyed a very successful year in fiscal 1987. The Systems Integration Industry expanded its share of deliveries of major corporate and government investments in computer and communications systems. Throughout the year, Systemhouse strengthened its position as a leader in this dynamic industry.

The financial performance of Systemhouse was strong in fiscal 1987. Revenues increased 68% to \$176.2 million from \$104.9 million in fiscal 1986, while net income increased 135% to \$23.7 million from \$10.1 million the year before. Earnings per share were up 86% to 93 cents compared with 50 cents in 1986.

While revenues and earnings were up for the year, business backlog and profit margins also improved, indicating a strong position for the 1988 business year. At the beginning of the 1987 year, backlog stood at \$148 million; entering 1988 the backlog was at \$240 million. Pretax income for the year was 13.6% of total revenues for 1987, up from 9.6% in 1986. With the strong order backlog and the continued flow of new business opportunities, this improved profit margin should be carried forward into 1988.

To deliver this increasing flow of business to our customers, Systemhouse needs a growing number of top quality employees who identify with the Systemhouse commitment to Systems Integration and to technology leadership. Our ability to retain the commitment of employees and to add to our total number of people gained momentum in 1987.

Part of this growth came through strategic acquisition following the integration of Capital Systems Inc., late in 1986. In 1987, the Company acquired DDC Consultants of Edmonton and DPLA of Montreal, giving us increased presence in the provinces of Alberta and Quebec. We also acquired ICT of Burlington, Massachusetts who bring us a core of expertise in the emerging fields of optical disk and image processing technology and Yipkon Corporation of Fairfield, N.J., who were extremely successful in selected U.S. Federal government accounts.

Employee turnover was slightly below that of last year. New people joined Systemhouse in the year to raise total employment to 1403 at year end, up from 1000 a year earlier. With the average number of employees for 1987 being 1164, revenue per employee for the year was \$151 thousand, up from \$139 thousand last year.

To accommodate this growth and to offer increased value to our customers, we have enhanced key aspects of our organizational and functional operations. New systems were implemented, highlighted by a leading edge office communications network. Internal training programs, particularly for our methodology and project management services have been expanded.

Finally, our relationships with hardware and software vendors emphasizing the communica-

tions orientation of the industry have been strengthened.

The Company also maintained its balance sheet to support future growth by adding \$24 million to equity as a result of net income for the year and a further \$62.1 million from the issue of common shares. Total shareholders' equity at year end was \$172.7 million, with working capital of \$141 million of which \$107 million was in





short term securities. This level of equity and liquidity will support total revenues of at least \$600 million before operations require further capital. This financial strength positions Systemhouse well to pursue aggressively the expanding commercial and government markets.

In 1987, the United States market accounted for about 60% of the Company's revenues. Canada accounted for 35% and international revenues were 5%. Canadian and international revenues were up 32% in the year, while U.S. revenues increased by 104%. The flow of business opportunities and our reputation for quality indicate continued strong revenue growth in 1988.

At mid-year, Systemhouse established a permanent branch in Los Angeles to serve that major marketplace. In late 1987, the incorporation of SHL Systemhouse S.A., with headquarters in Geneva, was completed. Permanent offices were established early in the current year, from which expansion of international business will be di-

rected. Experience gained internationally during this and the past two years will be of considerable value as these markets gain importance in 1988 and beyond.

All of us at Systemhouse are committed to quality for the customer and to building the leading company in our industry. To achieve these results, we must preserve an environment in which the best people in the industry want to participate. We must, at the same time, produce the results which ensure that the capital needed for growth continues to be available from investors who wish to share in our future. We see these not as opposing objectives, but as mutually interdependent and converging goals.

On behalf of all at Systemhouse we offer our thanks to our customers and our shareholders who have provided the basis for an outstanding year in 1987, and the confidence to expect another excellent year in 1988.



Peter A. Sandiford  
President & Chief Operating Officer

Roderick M. Bryden  
Chairman & Chief Executive Officer

# Business of the Company

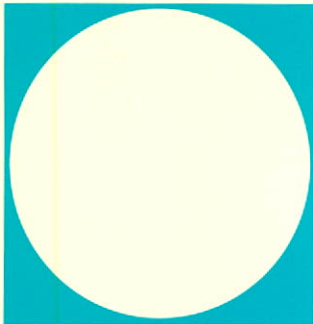
**S**ystemhouse delivers integrated information systems for commercial and government customers.

Systems integration can be represented as a channel. Product technologies, in the form of computer and communications hardware, as well as systems and application software products, are combined with custom software, project management skills and a range of implementation services to produce a unique system meeting each customer's specific requirements. We execute systems integration in system cycle phases — planning, design, construction, implementa-

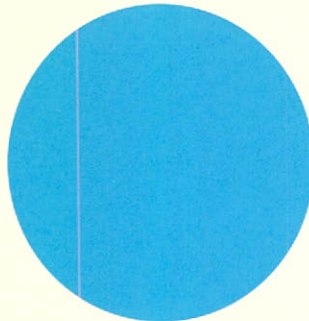
tion, and operations — with the aid of our comprehensive methodology covering each phase of the process. In this process, we deal with the organization's data, applications, and technology, both separately and as they must work together to create an integrated systems solution.

Every activity in the Company represents a commitment to quality. Our record of delivering large complex systems on time and for an agreed price — and what one industry analyst calls “the best user references in the industry” attest to this commitment.

## Planning



## Design



## Construction





# Value of Systems Integration

**T**he distinguishing feature of virtually every systems project is the need to integrate an array of products from a variety of vendors to achieve the function and performance required of the system.

As the responsible contractor for systems projects, Systemhouse offers value to customers in a variety of ways.

By assuming responsibility for the delivery of a system at a specified time, for an agreed upon price, Systemhouse minimizes technological and financial risks to the customer. This accountability ensures that the customer gets the system capability expected, when it is needed and at the cost on which the payback was based.

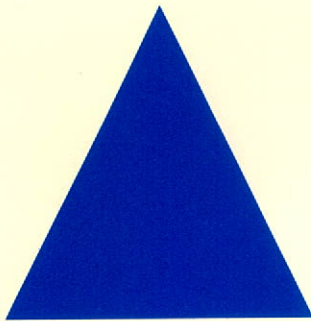
Systemhouse offers customers access to the latest and best technology available. From field experience to active participation on national and

on the capabilities and future directions of their products. Both our objectivity and broad experience assure customers of technological currency and the most appropriate solution.

Systems integration complements the MIS department's in-depth knowledge of the needs of the organization and the means by which technology can play a strategic role in meeting its objectives. Systemhouse works with the internal systems organization in delivering systems which are fully integrated into the corporation's technology base and future strategy.

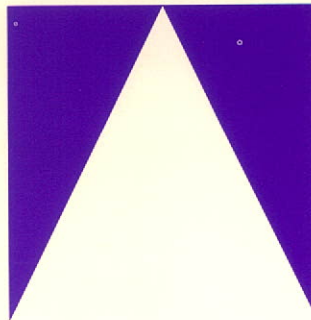
Control of complex projects is enhanced as major systems investments are delivered under a single supplier contract, with corresponding visibility by senior management. Objectives and scope are clearly defined and matched with a contracted cost and delivery timeframe. Clearly

## Implementation



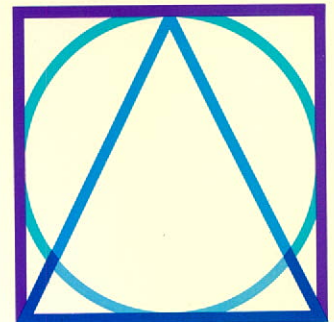
international standards committees and user groups, our professionals are constantly in touch with the best in technology methods and products. These efforts are complemented by technology suppliers who strive to keep us informed

## Operations

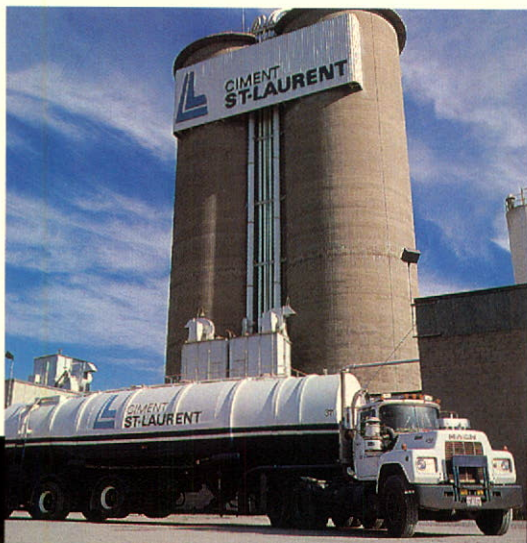


defined objectives for each of the users, MIS and Systemhouse combined with the contractually-defined decision processes facilitate harmonious relations and a continual focus on achieving the project's objectives.

## Integrated Systems







*Montreal-based St. Lawrence Cement, one of North America's largest producers and distributors of cement, called upon Systemhouse to develop a strategic long range systems plan to integrate regionalized operations. The DEC VAX-based systems will accommodate all financial and key operational systems for Quebec and Northeastern U.S. operations.*





# Planning

**Planning continues to grow in importance as customers seek to reduce risk, protect existing investments and secure maximum current and long range strategic value from information systems.**

**C**omprehensive planning for systems design, delivery and operations is the foundation on which a successful system is built. Planning continues to grow in importance as customers seek to reduce risk, protect existing investments and secure maximum current and long range strategic value from information systems.

The Systemhouse planning capability is an integrated process, taking into account an organization's current and desired data and applications together with the technologies required to support them. Paramount to the planning phase is the recognition of information as a tool in accomplishing the organization's goals. Guided by our methodology, planning activities include:

- analyzing business objectives, corporate strategies, and organizational philosophies together with existing business and regulatory environments;
- identifying strategic opportunities for the use of technology;

- analyzing business transactions and information flows;
- assessing the customer's current technical environment;
- producing hardware architectures and communications network plans;
- assessing organizational structures and management processes;
- preparing detailed project plans in accordance with operational and systems priorities;
- data analysis and modelling;
- site planning;
- conducting workshops, seminars, interviews, executive briefings.

Computer-Aided Software Engineering (CASE) tools are used to assist in organizing the extensive data gathered in the planning stages. In this way, knowledge gained in the early stages is available to be integrated in the more detailed analysis and design activities which follow. These tools support every aspect of the systems integration life cycle, enhancing productivity and ensuring consistency and integrity from planning through operations.

*As part of a logistics system to procure, inventory and distribute conventional ammunition for all Armed Services, Systemhouse helped plan, configure and deliver DSACS (Defense Standard Ammunition Computer System). The Amdahl-based system, managed by the U.S. Army HQ AMCCOM, emphasizes connectivity of hundreds of terminals and PC's to mainframes and the "wiring" of 17 administrative buildings at Army HQ on Rock Island, Illinois.*







Recognizing the Company's track record in human service delivery systems, the South Carolina Department of Social Services selected Systemhouse to plan and deliver the State's Client History and Information Profile System (CHIP). When completed, CHIP will provide eligibility information and produce benefits for Food Stamp and Aid to Families with Dependent Children programs through a network of 1,300 terminals and 66 department offices and central offices in Columbia.





# Design

**We configure a system which maximizes net benefits from technological change in a range of anticipated operational environments.**

**D**etailed analysis and design translate the requirements of the organization into a blueprint for the optimum system. The ultimate success of the system is determined by the extent to which the design matches the best of available technology and expertise with the unique requirements of the customer.

System designers and engineers consider the complete system — the growing number of applicable products, the software, the communications networks, equipment and carriers, and appropriate centralized or decentralized processing capability.

We configure a system which maximizes net benefits from technological change in a range of anticipated operational environments. Traditionally, prototypes have been used to facilitate the involvement of the user in defining his needs and finalizing the functionality of a system. More and

more frequently, as system complexity increases, there is a need for prototype systems and working models to ensure the operational integrity of the system and the compatibility of the various components.

Design considers the extent to which the customer's current investment in technology can be protected in the creation of a new system. We look at how new technologies and products can be introduced into the existing structures; what goes and what stays.

After specifying components and their functionality in the system, Systemhouse details how every aspect of the system will work together to create the desired result. The databases, screens and reports, the office and organizational procedures, the facilities and the communications networks are all specified in detail using automated design tools wherever applicable.

Finally, successful system design means predictable performance, — a system that will accommodate anticipated transaction volumes and be resilient to a range of changing circumstances. Use of advanced configuration and system performance tools and methodologies ensures the system will meet the objectives originally envisaged.

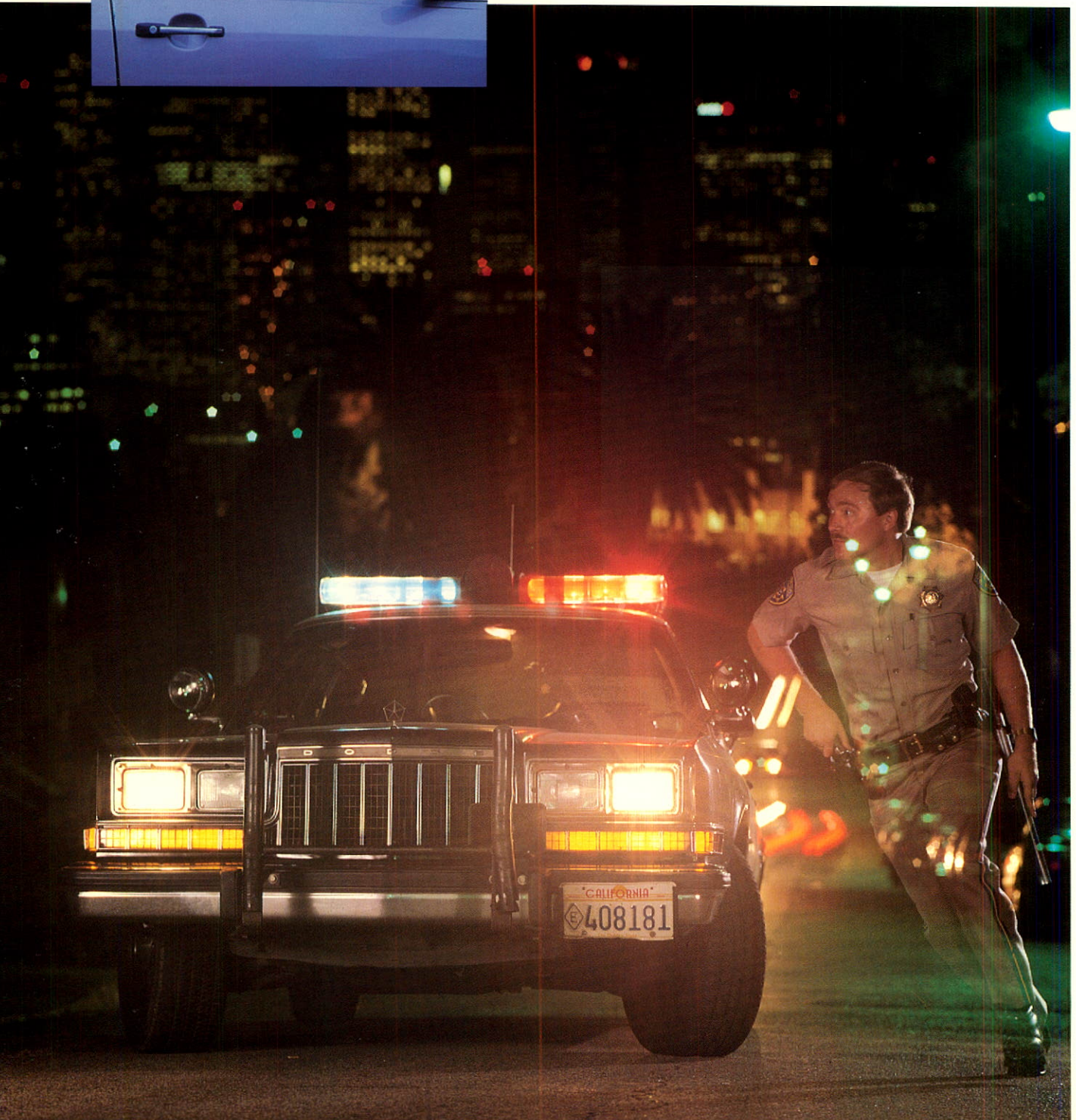
*For Chrysler's new \$764 million Bramalea plant, regarded as one of the most advanced automotive manufacturing facilities in North America, Systemhouse designed and implemented a Tandem-based Quality Assurance System. Approximately 350 programmable data terminals on the assembly line record and post defects for immediate action. Because the system does not interrupt the assembly process, productivity has increased while ensuring the highest possible quality in the manufacture of the upscale Eagle Premier.*







*Bell Cellular, the largest cellular mobile phone company in Ontario and Quebec, came to Systemhouse to meet their systems requirements to support their rapid business growth. The Company took full responsibility for acquiring and integrating IBM hardware and system software, financial software packages and extensive custom software development. The state-of-the-art on-line Customer Service and Billing system was implemented with minimum disruption enabling Bell Cellular to maintain its high level of customer service.*





# Construction

**The design prototypes and models are transformed into a fully functional system ready for introduction into the customer's operating environment.**

**T**he tangible evidence of the value of systems integration emerges as the construction activities commence. Now, the design prototypes and models are transformed into a fully functional system ready for introduction into the customer's operating environment.

Site locations are readied, vendor components are scheduled, delivered and installed. Each hardware and software component is tested for quality and performance. Where CASE tools were used earlier to analyze and design software, these same tools are often used to generate system documentation, data base structures and application software code where applicable. Design prototypes are brought up to production specification. Sub-contractors, where required, are applied to defined tasks, and arrangements are made for telephone, power and other essential services.

Where substantial custom software is required, programming teams, applying our rigorous software development methodology and operating within our detailed project management system, work together as a single unit to generate clear, error-free code on schedule to meet the specifications established in design. Extensive unit and system testing assure the functionality, viability and integrity of the custom software component.

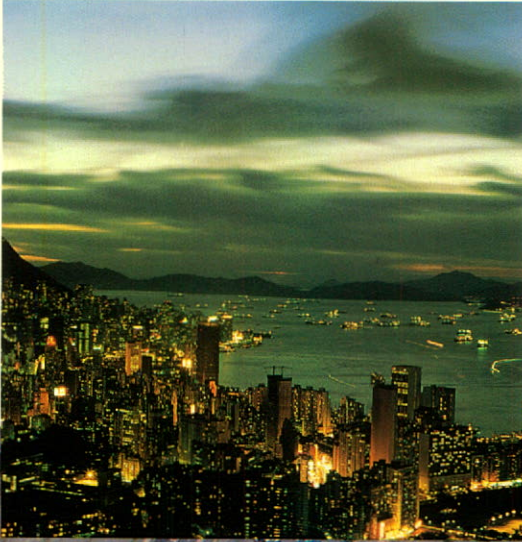
Once all component parts have been delivered, installed and tested, interfaces between the new systems and the customer's existing technology are tailored in preparation for integration into the customer's operations.

Finally, complete integration testing takes place in a simulated operational environment to ensure that the result meets the exacting standards established during the planning and design phases. All of this occurs under the direction and supervision of experienced Systemhouse project managers supported by the time-proven Systemhouse project management methodology.

*This year Systemhouse began building CJIS, the largest county criminal justice information system in the U.S. for Los Angeles County. Accessible by some 40,000 mobile and office terminals, the IBM mainframe-based CJIS will provide on-line information to such agencies as the District Attorney, Public Defender, County Sheriff, Probation Department and the Superior Court. The cornerstone of CJIS will be the custom software's ability to integrate transactions, allowing the updating of data across systems from a variety of hardware vendors.*







Experience in complex real-time systems and a track record of successful delivery internationally resulted in the Company's award for the delivery of an advanced vessel traffic management system to monitor ship movements in the port of Hong Kong, one of the busiest waterways in the world. State-of-the-art tracking and display equipment from Norcontrol Surveillance Systems A/S and VAX processors from Digital Equipment will be implemented by the Company together with integration and custom software services for the project delivered with DGB Consultants under the aegis of Canadian Commercial Corporation.





# Implementation

**Teamwork established between Systemhouse and the customer in planning and building the system has its greatest benefit as we work together to bring the system to life.**

**A** properly planned and executed implementation effort is as much a determinant of the eventual success of a system as are all the efforts that have gone on before to create the system. Here, the teamwork established between Systemhouse and the customer in planning and building the system has its greatest benefit as we work together to bring the system to life.

During the Implementation Phase, Systemhouse professionals organize training of operating personnel, in-house systems maintenance staff and end users. Briefing sessions are conducted for management and other staff to ensure optimum effectiveness during this critical transition period.

Final check-out of sites, fine tuning of software, delivery and installation of workstations, printers, terminals and other devices ensure that the physical environment is fully readied for operation.

Systemhouse professionals provide advice and guidance to customer staff in planning for acceptance testing, preparation of test data, scheduling of file and data conversion, and a host of other detail tasks required to get the system into a production mode. System acceptance is a major event for a customer as it is usually immediately followed by the system "going live". During this critical stage, fully trained staff are on duty to attend to any unanticipated problems and provide "life support" until the system is fully integrated into the customer's normal operations.

Customer staff and the Systemhouse team share a commitment to successful implementation.

*For one of the most complex financial systems in either the government or commercial sector, Systemhouse is providing the hardware and systems software for implementation, configuring and maintaining the US Navy Headquarters Programming and Budgeting systems. When fully implemented, they will be used in all aspects of the Navy Program Administration as the budget numbers for over 700 program elements are integrated and rolled up to the Secretary of the Navy. 125 Digital Equipment VAX systems will be installed by the Company, primarily at the Pentagon as well as in other Washington locations and in Hawaii and England.*







A corporate reorganization necessitated the recent move of Genstar Stone Products data processing headquarters from Dallas to Hunt Valley, Maryland. Systemhouse was contracted by the road building material supplier to set up and operate its new corporate data center. For the project, Systemhouse designed the facility, acquired the IBM computers, installed and tested all hardware and custom applications software, and manages day-to-day operations including maintenance and disaster recovery.





# Operations

**After implementation, Systemhouse responds to the customer's needs, from selected post-installation services to full operational management.**

**C**omplex systems increasingly demand more than a 'handover'. After implementation, Systemhouse responds to the customer's needs, from selected post-installation services to full operational management.

Systemhouse complements the capabilities within customers' organizations to ensure the system continues to deliver maximum benefits through its operational life cycle. Systemhouse provides a range of specialized services tailored precisely to the customer's continuing requirements. These include performance analysis and system tuning, integration of vendor hardware upgrades and software releases, telecommunications network management, and contingency planning and disaster recovery.

In full operations management contracts, Systemhouse delivers all aspects of the successful operation of the system. Contract pricing can either be fixed or transaction based. We operate systems at the customer site or at Systemhouse offices.

Post-installation services or full responsibility for systems operations offers the customer ready, ongoing access to continuous advances in computer and communications technology while controlling internal staff growth. Most importantly, it permits our customers to focus on managing their business rather than managing technology.

*For the Washington-based Office of Comptroller of the Currency, Systemhouse acquired the Amdahl hardware and system software for the client's new data center. Additionally, the Company supplied pre- and post-migration software support as the customer moved from a service bureau to their new facility.*





In an effort to more effectively retrieve and print standard documents, the U.S. Navy is using Systemhouse to deliver its NPODS (Navy Print on Demand System) project. Integrating recent optical disk storage technology from a variety of sources including Digital Equipment, Hitachi and Xerox, the system will ensure document currency and integrity while reducing storage space requirements from a warehouse the size of nine football fields to a 10 ft. X 10 ft. room.





# Technology

**The creation of technology is the business of hardware and software product vendors. The application of technology is the business of Systemhouse.**

**T**he creation of technology is the business of hardware and software product vendors. The application of technology is the business of Systemhouse. The link between the technology of the vendors and its successful application is the Systemhouse Technology Network.

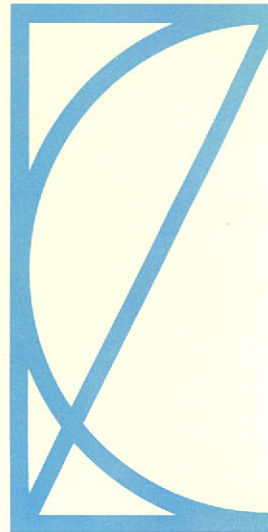
The Technology Network is a Company process that speeds the flow of product information from suppliers and encourages all employees to participate in monitoring and evaluating emerging technologies and their application.

Directed corporately, the Technology Network Program, comprised of a series of strategic technologies, is implemented in every branch by local professional staff. Its objective is the Company-wide promotion and dissemination of new product information and technological advances so that they can be applied effectively to the benefit of our customers.

In every location, members of Technology Networks are a part of a dynamic process of accumulating and absorbing technological information originating from vendors and others in the technology industry, and passing on that which is judged to be significant and valuable to the rest of the Company.

The end result is the application of cost-effective, high quality information technology products which meet the increasingly demanding requirements of industry and government for more and better information and information access mechanisms.

The Technology Network Program is a Systemhouse innovation that contributes to our goal of technology leadership.



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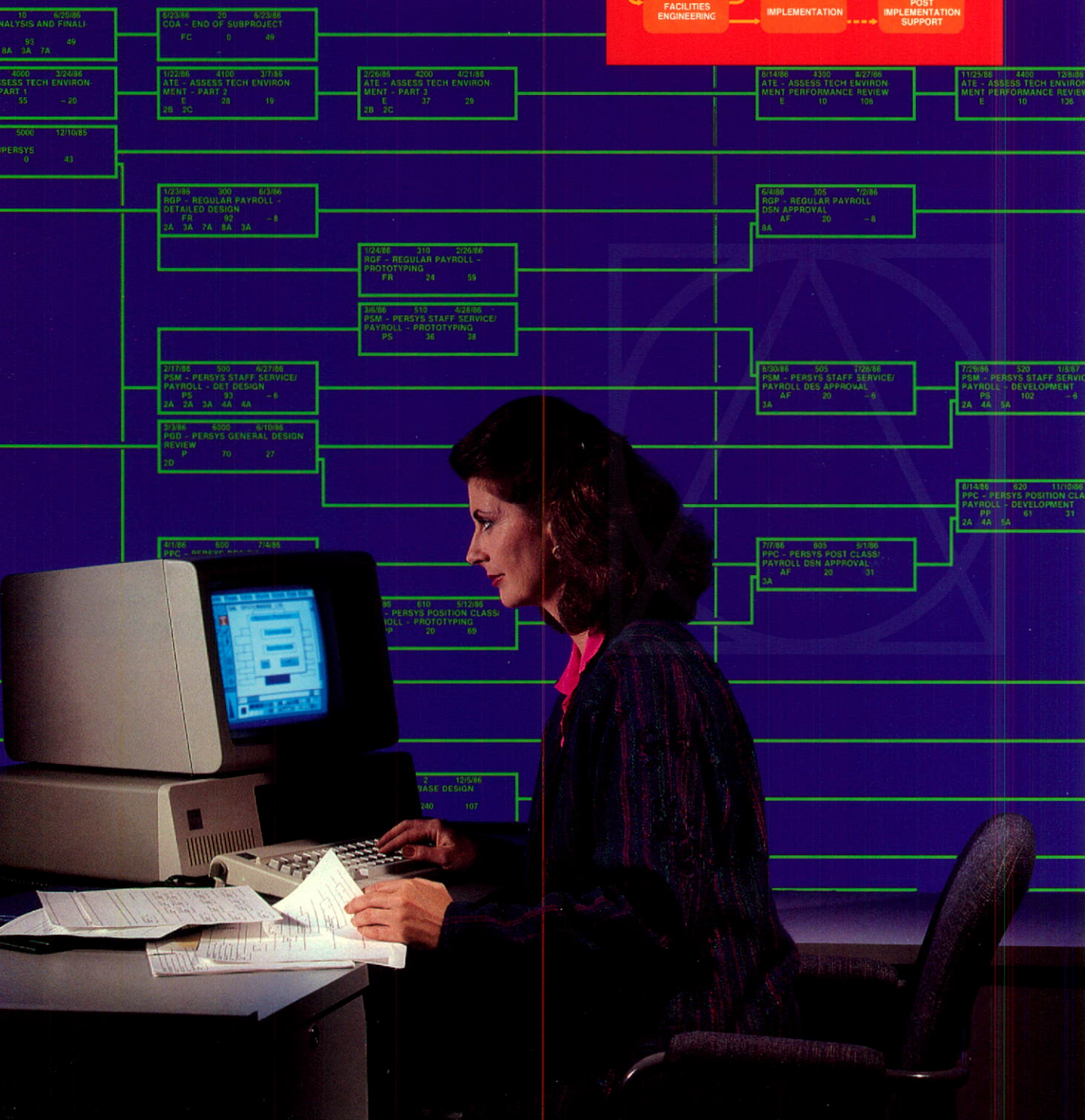
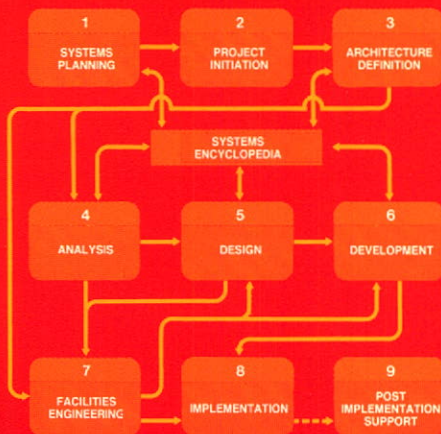
*The Company is supplying the Royal Canadian Mounted Police with one of the most technically advanced integrated data network systems in North America. Tandem Non Stop Processors will provide the RCMP with an upgraded communications environment for 4,000 remote devices, giving the RCMP, provincial and municipal law enforcement agencies across Canada instant access to databases in Ottawa.*





The critical element of the Company's success is SILC (Systems Integration Life Cycle), our proven methodology for building information systems.

# SYSTEMS INTEGRATION LIFE CYCLE





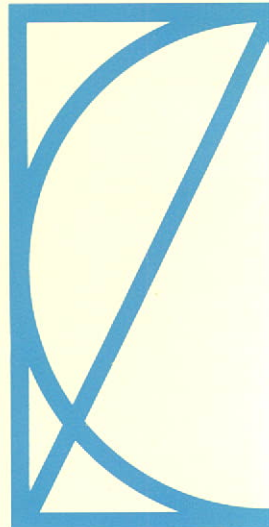
# Methodology

**SILC allows us to effectively plan the systems integration effort, to accurately predict the resulting delivery and operational costs, and to correctly anticipate the operational performance.**

**S**ILC (Systems Integration Life Cycle) is the Systemhouse methodology to ensure smooth delivery of complex systems. SILC is unique because it comes from the experience of systems professionals and captures the best techniques from thousands of person years of delivery effort over our 15 year history. It is enhanced continually as advances in methods and techniques are proven in the field by our staff of 1,500 people working in a multitude of technical and operational environments. SILC goes far beyond traditional system development methodologies encompassing not only the software development life cycle but also Project Management, Strategic Planning, Facilities Engineering, Quality Assurance, Architecture Definition, Capacity Planning and other disciplines essential to a successful systems integrator.

SILC is supported in all stages by a variety of CASE and system modelling tools selected as appropriate for the technical and customer environment.

Since we introduced the original Systems Development Life Cycle in the 1970's we have been at the forefront of the process of building systems. SILC reflects this experience which allows us to effectively plan the system integration effort, to accurately predict the resulting delivery and operational costs, and to correctly anticipate the operational performance of the system.



*SILC successfully governs the system design and development of complex projects such as the world-wide financial and personnel management systems for the Rome-based Food and Agriculture Organization of the United Nations.*





Systemhouse Baltimore branch's softball team participates in a friendly but competitive league with our customers including, the Social Security Administration and AT&T. Here, Pitcher/Business Center Manager, Harvey Pollack conducts a post game wrap-up with Maryland National Bank players.





# People

**Ultimately, our customers benefit  
from our low turnover rate  
and our highly motivated staff.**

**S**ystemhouse is committed to creating and maintaining the best work environment in the industry. Challenging projects on the leading edge of the application of new technologies, extensive in-house education and a management philosophy strongly focussed on career development combine to offer our staff virtually unlimited technical and management career growth.

Each Systemhouse professional is part of a business center; a functional unit which secures and delivers projects under the overall direction of Branch Management. These self-contained profit centers foster a spirit of entrepreneurship and a non-hierarchical structure which allows for dynamic, responsive operations.

In the Company's innovative Career and Education Management (CEM) Program, senior staff are Career Managers, each responsible for the careers of a small number of employees. The Career Manager is responsible for understanding each employee's aspirations, talents and accomplishments, creating a personalized program of

experience and education, and ensuring the attainment of employee goals as rapidly as possible. In this way, our people are able to grow with the Company, providing increased value to customers as their knowledge and competence expands.

Continued low staff turnover is evidence of our success in establishing mutual commitment between Systemhouse and our employees.

Despite limited career advertising, rare use of outside agencies, and no full-time internal recruiters, well over 1,000 professionals apply each month to Systemhouse. This suggests that our reputation as the best place to work in the industry is taking hold across North America.

Our large and growing core of long-term employees both create and absorb a unique corporate culture, psychology and practice, transferring these values to a growing staff complement through a highly supportive team environment.

Ultimately, our customers benefit from our low turnover rate and our highly motivated staff. This continuity and depth of skills forms the foundation for solid customer relationships and helps to assure the continuing success of systems projects.

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*One of the longest running customer relationships Systemhouse enjoys is with Great West Life. Since 1979, the Company has completed over 30 projects for the insurance firm. Pictured are Mike Parsons, Dale Hildebrandt, Janet Milne, and Dave Green leaving Great West Life headquarters in Winnipeg.*





# Locations

## Corporate Office — Canada

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General Manager

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General Manager

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# Consolidated Financial Statements

## Auditors' Report

### To the Shareholders of SHL Systemhouse Inc.:

We have examined the consolidated balance sheets of SHL Systemhouse Inc. as at August 31, 1987 and 1986 and the consolidated statements of operations, retained earnings and cash flows for each of the years in the three year period ended August 31, 1987. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at August 31, 1987 and 1986 and the results of its operations and the changes in its financial position for each of the years in the three year period ended August 31, 1987 in accordance with accounting principles generally accepted in Canada applied on a consistent basis during the period.



Clarkson Gordon  
Chartered Accountants  
A member of Arthur Young International

Ottawa, Canada,  
October 9, 1987.



# Consolidated Balance Sheets

(in thousands of Canadian dollars)

Assets	August 31	
	1987	1986
Current:		
Cash and short term deposits	\$ 107,021	\$ 51,150
Accounts receivable (note 3)	35,025	25,719
Work in process	37,758	16,782
Prepaid expenses	3,380	2,396
	183,184	96,047
Long term receivables	6,853	1,220
Fixed assets (note 4)	12,991	7,222
Goodwill (note 2)	17,792	10,626
	<u>\$ 220,820</u>	<u>\$ 115,115</u>

## Liabilities and Shareholders' Equity

Current:		
Accounts payable and accrued liabilities	\$ 30,500	\$ 20,490
Accrued employee costs	5,165	3,531
Current portion of long term debt	1,469	2,147
Deferred revenue	4,702	961
	41,836	27,129
Long term debt (note 5)	3,554	1,088
Deferred office lease inducements (note 5)	2,698	
Commitments and contingencies (note 12)		
Shareholders' equity (note 6):		
Common Shares		
Issued — 26,627,645 (1986 — 24,059,598)	143,384	76,158
Retained earnings, after a capital reduction of \$31,071 during 1983 and a further \$33,473 during 1985	31,321	10,740
Translation account (note 1 (e))	(1,973)	
	172,732	86,898
	<u>\$ 220,820</u>	<u>\$ 115,115</u>

On behalf of the Board:

Director



Director



(See accompanying notes to the consolidated financial statements)





# Consolidated Statements of Operations

(in thousands of Canadian dollars, except per share amounts)

	Years ended August 31				
	1987	1986	1985		
			Con- tinuing Opera- tions	Net Gain on Sale of Discon- tinued Opera- tions	Total
Gross revenue	\$ 168,576	\$ 102,080	\$ 48,744		\$ 48,744
Other income	7,609	2,846	1,545		1,545
Total revenue	176,185	104,926	50,289		50,289
Less cost of hardware and licensed software sold	71,234	45,940	13,597		13,597
Operating revenue	104,951	58,986	36,692		36,692
Expenses:					
Operating and administration	77,906	46,385	29,760		29,760
Depreciation and amortization	2,884	1,970	1,280		1,280
Interest	268	552	1,465		1,465
	81,058	48,907	32,505		32,505
Income before the following	23,893	10,079	4,187		4,187
Net gain on sale of discontinued operations (note 9)				\$ 4,795	4,795
Income before the following	23,893	10,079	4,187	4,795	8,982
Provision for income tax (note 8)	11,517	5,241	2,000	1,200	3,200
Income before benefit of loss carry forward	12,376	4,838	2,187	3,595	5,782
Benefit of loss carry forward (note 8)	11,369	5,241	2,000	1,200	3,200
Net income	\$ 23,745	\$ 10,079	\$ 4,187	\$ 4,795	\$ 8,982
Basic earnings per Common Share (note 10):					
Income before benefit of loss carry forward	\$ 0.49	\$ 0.24	\$ 0.15	\$ 0.25	\$ 0.40
Net income	\$ 0.93	\$ 0.50	\$ 0.29	\$ 0.33	\$ 0.62

(See accompanying notes to the consolidated financial statements)





# Consolidated Statements of Retained Earnings

(in thousands of Canadian dollars)

	Years ended August 31		
	1987	1986	1985
Retained earnings (deficit), beginning of year	\$ 10,740	\$ 6,352	\$ (34,543)
Net income	23,745	10,079	8,982
	34,485	16,431	(25,561)
Capital reduction (note 6(c))			33,473
Stock dividend on First Preference Shares (note 6(d))			(820)
Excess of cost of Common Shares purchased over proceeds			(106)
Premium on redemption of Common Shares (note 2)	(321)		
Share issue and other related costs	(2,843)	(5,691)	(634)
Retained earnings, end of year	\$ 31,321	\$ 10,740	\$ 6,352

(See accompanying notes to the consolidated financial statements)





# Consolidated Statements of Cash Flows

(in thousands of Canadian dollars)

	Years ended August 31		
	1987	1986	1985
<b>Operating Activities</b>			
Income before benefit of loss carry forward	\$ 12,376	\$ 4,838	\$ 5,782
Items not affecting cash:			
Depreciation and amortization	2,884	1,970	1,280
Provision for deferred income tax	11,369	5,241	3,200
Net gain on sale of discontinued operations			(4,795)
Other	959	(191)	(609)
Office lease inducements	1,495		
Net change in non-cash balances related to operations	(17,349)	(18,596)	(2,411)
Net cash provided by (applied to) operating activities	11,734	(6,738)	2,447
<b>Investing Activities</b>			
Purchases of fixed assets	(9,502)	(2,066)	(1,961)
Disposals of fixed assets	1,294	36	1,163
Increase in long term receivables (net)	(5,681)		
Acquisition of Yipkon Corporation (note 2)	(8,257)		
Acquisition of Capital Systems, Inc. (note 2)	388	(5,360)	
Net repayments by (advances to) affiliated company		2,207	(2,207)
Proceeds from sale of discontinued operations			8,000
Net cash provided by (applied to) investing activities	(21,758)	(5,183)	4,995
<b>Financing Activities</b>			
Issues of Common Shares (net)	64,062	64,547	3,963
Conversion of debentures			(3,600)
Stock dividend paid on First Preference Shares			(820)
Increase (decrease) in long term debt (net)	1,833	(1,612)	(190)
Net cash provided by (applied to) financing activities	65,895	62,935	(647)
Increase in cash and short term deposits	55,871	51,014	6,795
Cash and short term deposits, beginning of year	51,150	136	(6,659)
Cash and short term deposits, end of year	\$ 107,021	\$ 51,150	\$ 136

(See accompanying notes to the consolidated financial statements)





# Notes to the Consolidated Financial Statements

## 1. Summary of Significant Accounting Policies

These consolidated financial statements, which include the accounts of SHL Systemhouse Inc. and its wholly owned subsidiaries, have been prepared by management in accordance with accounting principles generally accepted in Canada consistently applied. These principles also conform in all material respects with accounting principles generally accepted in the United States except as described in note 7. Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of financial statements for a period necessarily involves the use of estimates and approximations which have been made using careful judgment. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

### a) Revenue recognition

Revenue is recognized on a percentage of completion basis whereby revenue and work in process are recorded at the estimated realizable value of work completed to date. Deferred revenue is recorded to the extent that billings to clients are in excess of revenue recognized to date.

### b) Fixed assets

Fixed assets are initially recorded at cost. Assets under capital lease are initially recorded at the present value of minimum future lease payments.

Depreciation and amortization are provided as set out below:

	RATE	BASIS
Furniture	10%	Declining balance
Office equipment	20%	Declining balance
Computer equipment	30%	Declining balance
Leasehold improvements	Term of lease	Straight line

### c) Goodwill

Goodwill is being amortized on a straight line basis over 40 years. The Company reviewed its estimate of the future benefits to be derived from the goodwill acquired on each acquisition made during fiscal 1986 and 1987, and determined that it equals or exceeds a period of 40 years. Accordingly, effective the fourth quarter of fiscal 1987, the Company prospectively extended its period of amortization of its goodwill to 40 years. The effect of this was to reduce the amortization of goodwill by \$320,000 in the fourth quarter.

### d) Income taxes

The Company follows the tax allocation method of accounting for income taxes. The Company accounts for investment tax credits using the cost reduction method, whereby tax credits related to qualifying expenditures are accrued and applied to reduce such expenses in the year in which they are incurred, provided there is reasonable assurance of realization.

### e) Foreign currency translation

Commencing in fiscal 1987, as a result of the significant expansion and resulting self-sustaining nature of its U.S. subsidiary, the Company prospectively adopted the current rate method of foreign currency translation. Under this method, assets and liabilities are translated at the exchange rate in effect on the balance sheet date, and revenues and expenses are translated at the average exchange rate in effect during the period. Cumulative translation adjustments are deferred in a separate component of shareholders' equity called the Translation account.



## 2. Acquisitions

On April 30, 1986 and January 31, 1987, the Company acquired all the outstanding capital stock of Capital Systems, Inc. ("CSI") and Yipkon Corporation ("Yipkon"), respectively. These acquisitions were accounted for using the purchase method. The results of operations for CSI and Yipkon have been included in the consolidated financial statements from May 1, 1986 and February 2, 1987, respectively.

CSI and Yipkon, private corporations incorporated in the United States, are engaged in the computer systems integration business. The assets acquired and assigned values were:

### (a) CSI

	(000's)
Ascribed value of 720,000 Common Shares issued	<u>\$4,464</u>
Net liabilities assumed:	
Working capital deficiency, including costs of acquisition of \$896,000	6,922
Fixed assets	(2,344)
Long term debt	<u>1,719</u>
	<u>6,297</u>
Goodwill	<u><u>\$10,761</u></u>

Pursuant to the purchase agreement, the selling shareholders agreed to indemnify the Company

against certain claims. To secure these claims 352,800 Common Shares were deposited in escrow. In February 1987, all claims were settled and 12,590 Common Shares, previously held in escrow, were cancelled for consideration totalling approximately \$388,000 (U.S. \$288,000).

### (b) Yipkon

	(000's)
Cash consideration	<u>\$7,433</u>
Net liabilities assumed:	
Assets acquired, including costs of acquisition of \$824,000	(8,797)
Liabilities assumed	<u>8,870</u>
	<u>73</u>
Goodwill	<u><u>\$7,506</u></u>

The following unaudited pro forma financial information gives effect to the acquisitions of CSI and Yipkon as if (i) for the year ended August 31, 1985, CSI was acquired on September 1, 1984, (ii) for the year ended August 31, 1986, CSI and Yipkon were acquired on September 1, 1985 and, (iii) for the year ended August 31, 1987, Yipkon was acquired on September 1, 1986.

	Unaudited (000's except per share amounts) Years ended August 31		
	1987	1986	1985
Total revenue	\$188,571	\$141,922	\$83,624
Income before benefit of loss carry forward	9,587	1,155	1,346
Net income	21,484	3,769	3,346
Earnings per Common Share:			
Income before benefit of loss carry forward	\$ 0.38	\$ 0.06	\$ 0.09
Net income	\$ 0.84	\$ 0.18	\$ 0.22

The pro forma financial information for the year end August 31, 1985 includes the Company's continuing operations only.

## 3. Accounts Receivable

Included in accounts receivable is an allowance for doubtful accounts of \$1,516,000 (1986 — \$2,224,000).





#### 4. Fixed Assets

(000's) August 31				
		1987	1986	
	Cost	Accumulated depreciation	Net	Net
Furniture and office equipment	\$ 4,672	\$ 1,505	\$ 3,167	\$ 900
Computer equipment	12,132	3,464	8,668	4,123
Leasehold improvements	1,671	924	747	438
Assets under capital lease:				
Furniture and office equipment	438	213	225	817
Computer equipment	315	131	184	944
	<u>\$19,228</u>	<u>\$ 6,237</u>	<u>\$12,991</u>	<u>\$ 7,222</u>

Accumulated depreciation as at August 31, 1986 amounted to \$5,301,000.

#### 5. Long Term Debt

(000's) August 31		
	1987	1986
Capital lease obligations bearing interest at rates varying from 12% to 21.5% (including 1987 — U.S. \$3,711,000; 1986 — U.S. \$756,000)	\$ 4,924	\$ 2,266
Other	99	969
	5,023	3,235
Less current portion	(1,469)	(2,147)
	<u>\$ 3,554</u>	<u>\$ 1,088</u>

During the year ended August 31, 1987, the Company incurred operating lease expenses of approximately \$5,107,000 (1986 — \$3,068,000; 1985 — \$2,506,000).

The Company is committed to make future minimum payments on leases as follows:

(000's) August 31, 1987		
	Capital Leases	Operating Leases
1988	\$ 1,718	\$ 4,694
1989	1,528	4,545
1990	1,471	4,248
1991	1,362	3,301
1992	30	2,295
	6,109	\$ 19,083
Less interest	(1,185)	
	<u>\$ 4,924</u>	

The deferred office lease inducements are being amortized over the term of the lease, 10 years.





## 6. Capital Stock

The Company's authorized share capital consists of an unlimited number of Common Shares without nominal or par value and an unlimited number of First Preference Shares issuable in series. During the year ended August 31, 1987, a Certificate of Amendment was issued subdividing the Common Shares on a two-for-one basis. All share amounts in these financial statements reflect this adjustment.

A summary of the changes during the period August 31, 1984 to August 31, 1987, in issued and fully paid First Preference Shares, Class A Common Shares, and Common Shares is as follows:

	(000's except share amounts)					
	First Preference Shares		Class A Common Shares		Common Shares	
	Number of Shares	Amount	Number of Shares	Amount	Number of Shares	Amount
Balance, August 31, 1984	5,357,154	\$ 26,786	17,641,925	\$ 8,187		
Conversion of Debentures (a)			3,130,434	3,600		
Change of First Preference Shares (b)	(5,357,154)	(26,786)	16,071,462	26,786		
Capital Reduction (c)				(33,473)		
Payment of stock dividend (d)			546,631	820		
Change in Class A Common Shares to Common Shares (e)			(37,390,452)	(5,920)	14,956,094	\$ 5,920
Balance, August 31, 1985	—	\$ —	—	\$ —	14,956,094	5,920
Issued in public offerings (f)					8,200,000	64,875
Employee Stock Purchase Plan					38,634	259
Stock options exercised					84,940	430
Bank warrants exercised (g)					60,000	210
Issued to acquire Capital Systems, Inc. (note 2)					720,000	4,464
Payments in lieu of fractional shares					(70)	
Balance, August 31, 1986					24,059,598	76,158
Issued in public offering and private placement (f)					2,465,000	64,943
Employee Stock Purchase Plan					115,654	2,350
Settlement of acquisition of Capital Systems, Inc. (note 2)					(12,590)	(67)
Payments in lieu of fractional shares					(17)	
Balance, August 31, 1987					26,627,645	\$ 143,384

- (a) Upon payment by the Company of \$180,000 during January 1985, to the holders of outstanding debentures, these debentures were converted into 3,130,434 Class A Common Shares.
- (b) During the year ended August 31, 1985, the Series 1 Convertible Redeemable First Preference Shares were changed into Class A Common Shares on a 3 for 1 basis.
- (c) During the year ended August 31, 1985, the shareholders approved a reduction of \$33,473,000 to stated capital and deficit.
- (d) During the year ended August 31, 1985, the Company declared and paid a dividend of \$820,000 on the 2,910,551 First Preference Shares owned by an affiliated company relating to the period prior to April 15, 1983 during which time an affiliate's funds were invested in the Company. This dividend was paid through the issue of 546,631 Class A Common Shares.
- (e) During the year ended August 31, 1985, there was a change of Class A Common Shares into Common Shares and a consolidation of the resulting Common Shares on the basis of one new share for five old shares. All share amounts in these financial statements reflect this adjustment
- (f) During the year ended August 31, 1986, the Company issued 8,200,000 Common Shares from treasury for gross proceeds of \$64.9 million in two separate public issues. During the year ended

August 31, 1987, the Company issued 1,684,550 Common Shares to the public for gross proceeds of \$45.1 million and 780,450 Common Shares to an affiliated company in a private placement for gross proceeds of \$19.8 million. The purchase price of the Common Shares sold to the affiliate was equal to the public offering price less underwriting fees.

- (g) Under a banking agreement, the Company had granted the Company's banker warrants to purchase 60,000 Common Shares at \$3.50 per share. During the year ended August 31, 1986, the bank exercised all these warrants.

### **Employee Share Plans**

Pursuant to the Employee Stock Purchase Plan, employees are eligible to acquire Common Shares within certain limits at amounts based on market prices.

During the year ended August 31, 1987, the Company granted options to certain executive and senior employees to purchase 357,900 Common Shares at prices ranging from \$11.00 to \$29.25 per share. These options may be exercised from September 1, 1989 to February 28, 1990.

At August 31, 1987, a total of 981,900 options to purchase Common Shares were outstanding at prices ranging from \$2.00 to \$29.25 per share which are eligible to be exercised at various dates from September 1, 1987 to February 28, 1990.



## 7. United States Accounting Principles

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada which conform, in all material respects, with accounting principles generally accepted in the United States ("U.S. GAAP") for the periods presented except for the

calculation of earnings per Common Share. The following table presents the earnings per Common Share determined in accordance with U.S. GAAP, which reflects the application of the treasury stock method for outstanding options and warrants:

	Years ended August 31		
	1987	1986	1985
Primary earnings per Common Share:			
Continuing operations:			
Before extraordinary item _____	\$0.47	\$0.24	\$0.15
After the benefit of loss carry forward _____	\$0.91	\$0.49	\$0.29
Discontinued operations _____			\$0.33
Net income _____	\$0.91	\$0.49	\$0.62 (i)
Fully diluted earnings per Common Share:			
Continuing operations:			
Before extraordinary item _____	\$0.47	\$0.24	\$0.14 (ii)
After the benefit of loss carry forward _____	\$0.91	\$0.49	\$0.28 (ii)
Discontinued operations _____			\$0.31 (ii)
Net income _____	\$0.91	\$0.49	\$0.59 (ii)

- (i) pro forma earnings per Common Share for the year ended August 31, 1985, had the debentures (note 6(a)) been converted into Common Shares on September 1, 1984 in conformity with U.S. GAAP, would have been \$0.60
- (ii) after reflecting the debentures as having been converted on September 1, 1984

## 8. Income Tax Information

The provision for tax reported differs from the amount computed by applying Canadian tax rates to income before taxes as follows:

	(000's) Years ended August 31		
	1987	1986	1985
Expected statutory tax rate _____	51%	52%	51%
Expected tax provision _____	\$12,185	\$5,241	\$4,581
Non taxable portion of capital gains _____			(1,381)
Lower tax rate in foreign jurisdictions _____	(668)		
Provision for income taxes reflected in the consolidated statements of operations _____	<u>\$11,517</u>	<u>\$5,241</u>	<u>\$3,200</u>

The Company has loss carry forwards as at August 31, 1987, for which no accounting benefit has been recognized, of approximately \$15 million of which \$9 million expires at various dates up to 2001 in the United States. The balance relates to Canada and may be carried forward indefinitely. In addition, the Company has timing differences of approximately \$5 million for which no accounting benefit has been recognized.

Income before tax attributable to the U.S. operation is as follows: year ended August 31, 1987 — \$7,637,000; 1986 — \$3,117,000; 1985 — \$11,000.

During the year, the Company recorded \$112,000 of investment tax credits as a reduction of operating and administration expenses (1986 — \$296,000; 1985 — \$422,000).

## 9. Related Party Transactions

- (a) As of September 1, 1984, the Company sold all of the shares of its wholly-owned Canadian subsidiaries (the "Canadian Subsidiaries") engaged in the software product business. These shares were sold to Kinburn Technology Corporation ("KTC"), which owns approximately 32% of the shares of the Company as at August 31, 1987, for an aggregate sale price of \$8 million cash. Upon the sale of the Canadian Subsidiaries to KTC, the Company recorded a gain of approximately \$4,795,000 net of fees and costs relating to the sale.

At August 31, 1985, the Company had outstanding \$2.2 million from KTC, which was repaid prior to February 28, 1986. Outstanding amounts, including intercompany balances included in (k) below, bear interest at bank prime plus 1%. Interest earned by the Company on these amounts for the year ended August 31, 1987 totalled approximately \$306,000 (1986 — \$400,000; 1985 — \$548,000) and is included in other income in the consolidated statements of operations.

- (b) One of the Canadian Subsidiaries advanced \$3.6 million to the Company during September 1984 without interest, which amount was repaid upon closing the sale of the Canadian Subsidiaries in January 1985.
- (c) The Company undertook development work for affiliated companies and during the year ended August 31, 1987 earned revenue of approximately \$5,323,000 (1986 — \$5,959,000; 1985 — \$2,755,000).
- (d) The Company obtained the rights to the use of the results of the development work referred to in (c) above and, during the year ended August 31, 1987, incurred \$3,087,000 (1986 — \$3,456,000; 1985 — \$1,598,000) in license fees of which \$1,323,000 was prepaid on October 24, 1986.





- (e) The Company received management services from an affiliated company during the year ended August 31, 1987, for a fee of \$170,000 (1986 — \$450,000; 1985 — \$166,000). Of this total \$50,000 (1986 — \$310,000) relates to services provided in connection with the public issues of Common Shares during these years.
- (f) The Canadian subsidiary referred to in (b) above agreed to bear the cost of interest on the Company's \$3,759,000 Part VIII tax liability commencing September 1, 1984, as this cost relates to research and development financing. Such interest earned totalled approximately \$492,000 for the year ended August 31, 1985, and is included in other income in the consolidated statements of operations.
- (g) The Canadian subsidiary referred to in (b) above agreed to bear the cost of interest of \$175,000 on the debentures referred to in note 6(a).
- (h) During the year ended August 31, 1985, the Company realized a gain of \$518,000 resulting from a purchase and sale and lease-back of office facilities with third parties. The Company sublet such facilities under similar terms to KTC. The lease and related sublease were cancelled in December 1985.
- (i) The Company provided certain administrative services to affiliated companies during the year ended August 31, 1986 for \$128,000 (1985 — \$115,000). No services were provided to these affiliated companies during the year ended August 31, 1987.
- (j) As of September 1, 1984, the Company sublet certain office furniture and equipment for a two year term, after which ownership of the assets transferred to affiliated companies. Interest earned on these capital leases during the year ended August 31, 1986 totalled approximately \$49,000 (1985 — \$117,000).
- (k) At August 31, 1987, the Company had intercompany balances included in accounts receivable in the consolidated balance sheets, totalling \$1,640,000 due from affiliated companies (1986 — \$715,000). During the year ended August 31, 1986, the Company advanced up to \$1,700,000 to KTC for which interest totalling \$45,000 was charged at the rate of bank prime plus 1%. These advances were repaid prior to March 1986.
- (l) In May 1987, the Company and KTC entered into an agreement with respect to the public offering by KTC of its U.S. \$90,000,000 principal amount of 9% Exchangeable Secured Subordinated Debentures due 2007. KTC agreed to pay to the Company a fee of \$300,000 and to reimburse the Company for certain costs incurred by the Company in connection with such public offering.
- (m) During the year ended August 31, 1987 the Company purchased equipment from affiliated companies for approximately \$1.1 million.

## 10. Earnings Per Share

The earnings per Common Share are calculated using the weighted average number of Common Shares outstanding during the respective fiscal year (1987 — 25,454,230; 1986 — 20,143,230; 1985 — 14,401,036).

Adjusted basic earnings per Common Share for the year ended August 31, 1985 would be \$0.60 if the

debentures referred to in note 6(a) were treated as having been converted on September 1, 1984.

There were no materially dilutive effects of the options outstanding for the years ended August 31, 1987 and 1986. Fully diluted earnings per Common Share for the year ended August 31, 1985 are as follows:

	Continuing Operations	Net Gain on Sale of Discontinued Operations	Total
Income before benefit of loss carry forward _____	\$0.15	\$0.23	\$0.38
Net income _____	\$0.28	\$0.31	\$0.59



## 11. Segmented Information

In the opinion of management, the Company currently operates in a single industry segment, being the computer systems integration business. This business involves the design, development, integration and implementation of computer-based information systems.

The Company carries on business primarily in two geographic segments, Canada and the United States.

Canadian-based sales to customers in foreign countries are as follows: year ended August 31, 1987 — \$13.6 million; 1986 — \$4.0 million; 1985 — \$1.7 million.

	(000's)					
	Years ended August 31					
	1987		1986		1985	
					Continuing Operations	
	Canada	U.S.	Canada	U.S.	Canada	U.S.
Gross revenue	<u>\$61,543</u>	<u>\$107,033</u>	<u>\$49,689</u>	<u>\$52,391</u>	<u>\$35,490</u>	<u>\$13,254</u>
Net income (i)	<u>\$12,292</u>	<u>\$ 10,797</u>	<u>\$ 6,833</u>	<u>\$ 4,439</u>	<u>\$ 4,886</u>	<u>\$ 194</u>
Depreciation and amortization	<u>\$ 1,424</u>	<u>\$ 1,460</u>	<u>\$ 1,296</u>	<u>\$ 674</u>	<u>\$ 1,142</u>	<u>\$ 138</u>
Total assets (ii)	<u>\$47,620</u>	<u>\$ 92,934</u>	<u>\$67,538</u>	<u>\$47,577</u>	<u>\$16,910</u>	<u>\$ 4,854</u>

(i) excludes Other income and general corporate expenses of \$656,000 in 1987 (1986 — \$(1,193,000); 1985 — \$(893,000))

(ii) as at August 31, 1987, the Company had approximately \$80 million of assets, primarily composed of cash and Canadian short term deposits, in a

wholly owned subsidiary located in Switzerland. These assets were transferred from Canada in conjunction with the commencement of operations in Switzerland. Income earned in Switzerland for the year ended August 31, 1987 was insignificant

Revenues generated from U.S. government agencies in fiscal 1987 amounted to approximately \$80.8 million (1986 — \$23.7 million; 1985 — \$3.0 million); from ministries and departments of the federal government

of Canada, approximately \$12.5 million (1986 — \$13.1 million; 1985 — \$8.0 million); and from Canadian federal crown corporations, approximately \$2.7 million (1986 — \$2.2 million; 1985 — \$2.8 million).



## 12. Commitments and Contingencies

### a) Litigation

The Company is involved in various litigation arising from the normal course of business. In the opinion of management, any adverse outcome to this litigation would not have a material effect on the consolidated financial statements of the Company.

### b) Performance Guarantees

As at August 31, 1987, the Company had approximately \$6.0 million of security deposits and letters of credit outstanding as required under certain contracts.

Short term deposits of \$2.7 million are pledged as collateral for security deposits and the Company has given a general assignment of book debts in connection with the letters of credit.

### c) United States Government Audits

Certain of the Company's U.S. government contracts are subject to subsequent audit of direct and indirect costs by an agency of the U.S. government. Management does not anticipate any material adjustment to the consolidated financial statements as a result of such audits.

### d) Part VIII Tax Liability

During the year ended August 31, 1984, the Company recognized funding from the sale of tax credits related to research and development expenditures. Such sale gave rise to a refundable tax liability of \$8.7 million.

The Company believes it has discharged this Part VIII tax liability by way of qualifying scientific

research expenditures and purchases of scientific research tax credits, resulting in a gain of approximately \$475,000 in fiscal 1985.

The qualified scientific research expenditures, the purchase of scientific research tax credits and the resulting Part VIII tax recovery are subject to review by Revenue Canada, Taxation. While Revenue Canada, Taxation has neither formally accepted nor reviewed in detail the eligible expenditures claimed by the Company, the Company has discussed with Revenue Canada the principles applied in administering its research and development program and believes that its obligations have been fully discharged.

### e) Interest Rate Swap Agreements

During the year ended August 31, 1986, the Company entered into an interest rate swap agreement which was accounted for as an investment. During November 1986, the Company terminated this agreement and realized a gain of \$670,000 which has been included in other income.

During February 1987, the Company entered into another interest rate swap agreement, which has been accounted for as a hedge of a portion of its investment portfolio, whereby the interest income on \$50 million has been fixed for five years at 8.99%. As part of the current agreement, the Company was required to provide \$4.5 million of short term deposits as collateral for the term of the agreement.

## 13. Consolidated Statements of Cash Flows

The Company has replaced the consolidated statements of changes in financial position, which accounted for changes in working capital, with the consolidated statements of cash flows, which account

for changes in cash and short term deposits. This change, which conforms to recommendations of the Canadian Institute of Chartered Accountants, has been adopted retroactively.





# Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company's Consolidated Financial Statements are prepared in accordance with Canadian generally accepted accounting principles which conform, in all material respects, with U.S. generally accepted accounting principles (see note 7 of the Notes to the Consolidated Financial Statements).

## Results of Operations For the three year period ended August 31, 1987

Total revenue for the Company for fiscal 1987 was \$176.2 million, an increase of 68% from total revenue of \$104.9 million in fiscal 1986, and an increase of 250% over total revenue from continuing operations of \$50.3 million for fiscal 1985. Total revenue in fiscal 1987 included other income of \$7.6 million. This consisted primarily of interest income from the investments held during the year. The increase in total revenue in fiscal 1987 is primarily attributed to expanded business volume through normal growth and the acquisitions discussed in note 2 of the Notes to the Consolidated Financial Statements.

The systems integration services provided by the Company may include procurement of computer hardware and software from suppliers at discounts. Costs of hardware and licensed software sold was \$71.2 million, or 42% of gross revenue in fiscal 1987, \$45.9 million, or 45% of gross revenue in fiscal 1986 and \$13.6 million, or 28% of gross revenue from continuing operations in fiscal 1985.

Operating and administration expenses were \$77.9 million, or 46% of gross revenue in fiscal 1987 compared with \$46.4 million or 45% of gross revenue in fiscal 1986 and \$29.8 million or 61% of gross revenue

from continuing operations in fiscal 1985. The increase in total operating and administrative expenses in fiscal 1987 and 1986 resulted primarily from increased employee costs attributable to an increase in the number of professional staff. Operating and administration expenses have decreased as a percentage of gross revenue from 61% in fiscal 1985 to 45% and 46% in fiscal 1986 and 1987, respectively. This is due largely to fixed price systems integration contracts which have higher hardware and software revenue components which require less operating and administration expenditures.

Depreciation and amortization expense increased 46% over fiscal 1986 and 125% over fiscal 1985. This increase reflects depreciation of computer equipment acquired during the year to service increased staff and customer requirements, as well as the increased assets acquired on the purchase of Capital Systems, Inc. and amortization of goodwill.

The provision for income tax for the year ended August 31, 1987 was not fully offset by benefits of losses carried forward from previous years due primarily to certain U.S. state income taxes which do not allow for the carry forward of previous years' losses.

At the end of fiscal 1987 the company had available tax loss carry forwards and timing differences of approximately \$20 million available to reduce taxable income in future years. The tax loss carry forwards are expected to be fully utilized during fiscal 1988.

Net income for fiscal 1987 was \$23.7 million, or 13% of total revenue. Net income for fiscal 1986 was \$10.1 million or 10% of total revenue. Net income from continuing operations for fiscal 1985 was \$4.2 million, or 8% of total revenue from continuing operations.



## Geographic Segments

Total revenue generated in the United States in fiscal 1987 was \$107.3 million, which represented 61% of the Company's total revenue in fiscal 1987 compared with \$52.7 million in fiscal 1986, which represented 50% of the Company's total revenue in fiscal 1986, and \$13.3 million from continuing operations in fiscal 1985, which represented 26% of the Company's total revenue from continuing operations in fiscal 1985. The balance of the total revenue in each of the above years was generated in Canada.

The increase in revenue in the United States over these years can be attributed to the growth in the

established branches and the acquisitions of Capital Systems, Inc. and Yipkon Corporation.

The Company has established a subsidiary company in Geneva, Switzerland from which its international operations will be conducted commencing fiscal 1988. For fiscal 1987 revenue from international projects was \$6.0 million compared with \$4.0 million in fiscal 1986 and \$1.7 million in 1985. These revenues are included in Canadian revenue.

## Liquidity and Capital Resources

At August 31, 1987, working capital was \$141.3 million compared with working capital of \$68.9 million at August 31, 1986. This increase in working capital of \$72.4 million is primarily reflected in an increase in cash and short term deposits of \$55.9 million, in work in process of \$21.0 million, and in accounts receivable of \$9.3 million, offset by increases in accounts payable and accrued liabilities of \$10.0 million, in deferred revenue of \$3.7 million, and in accrued employee costs of \$1.6 million.

The increase in cash and short term deposits of \$55.9 million is primarily due to the public share issue which generated \$62.1 million, net of share issue costs.

The increases in accounts receivable, work in process, accounts payable and accrued liabilities, accrued employee costs and deferred revenue all reflect increased business volume.

The systems integration business is not capital intensive as office premises are generally leased. The Company has no commitments to make any material capital expenditures in the 1988 fiscal year. Working capital is adequate for the Company's business through the next fiscal year and cash flow anticipated from operations in fiscal 1988 is expected to further improve the Company's liquidity.

In fiscal 1987, 1986 and 1985, the Company believes that inflation did not have a material impact on operating results. The Company's current practice of using separate contracts for each stage of a long-term engagement provides protection against escalating employee related costs. Computer hardware costs have not been sensitive to inflationary pressures.

## Quarterly Results

(000's except per share amounts)

(unaudited)

	<u>First Quarter</u>	<u>(1) Second Quarter</u>	<u>(1) Third Quarter</u>	<u>(1)(2) Fourth Quarter</u>
<b>Fiscal 1987</b>				
Total revenue	\$33,811	\$35,499	\$50,283	\$56,592
Operating revenue	21,653	23,688	28,000	31,610
Expenses	17,348	17,972	21,446	24,292
Income before benefit of loss carry forward	2,066	2,744	3,146	4,420
Net income	4,305	5,716	6,419	7,305
Basic earnings per Common Share:				
Before benefit of loss carry forward	0.09	0.11	0.12	0.17
Net income	0.18	0.23	0.24	0.27
			<u>(3) Third Quarter</u>	<u>(3) Fourth Quarter</u>
<b>Fiscal 1986</b>	<u>First Quarter</u>	<u>Second Quarter</u>		
Total revenue	\$16,808	\$19,846	\$23,665	\$44,607
Operating revenue	10,634	11,936	15,277	21,139
Expenses	9,424	10,021	12,574	16,888
Income before benefit of loss carry forward	593	938	1,304	2,003
Net income	1,210	1,915	2,703	4,251
Basic earnings per Common Share:				
Before benefit of loss carry forward	0.04	0.05	0.06	0.09
Net income	0.08	0.09	0.13	0.18

(1) Includes the results of Yipkon Corporation from February 2, 1987. Current rate method of foreign currency translation adopted in the second quarter of fiscal 1987.

(2) Amortization of goodwill extended to 40 years in the fourth quarter of fiscal 1987.

(3) Includes the results of Capital Systems, Inc. from May 1, 1986.





# Selected Financial Data

The following table summarizes certain selected consolidated financial information and is qualified in its entirety by, and should be read in conjunction with, the more detailed consolidated financial statements and related notes of the Company. The following table has been derived from the Company's consolidated financial statements which have been prepared in accordance with generally accepted accounting principles as applied in Canada ("Cdn. GAAP").

These principles are also in conformity, in all material respects, with generally accepted accounting prin-

ciples as applied in the United States ("U.S. GAAP") except with respect to (i) deferral of software product development cost, (ii) the presentation in the balance sheet of the First Preference Shares, (iii) the presentation of the gain on disposal of discontinued operations, and (iv) the calculation of earnings per share (see the footnotes to the following table and note 7 of the Notes to the Consolidated Financial Statements).

(000's except share and per share amounts)									
Years ended August 31									
	1987(2)	1986(2)	1985			1984		1983(1)	
			Continuing Operations	Net gain on sale of Discontinued Operations	Total	Continuing Operations	Discontinued Operations(1)	Total(1)	
<b>Income Statement Data:</b>									
Total Revenue	\$176,185	\$104,926	\$50,289		\$50,289	\$36,338	\$21,095	\$57,433	\$49,815
Operating revenue	\$104,951	\$58,986	\$36,692		\$36,692	\$26,365	\$10,645	\$37,010	\$34,381
Expenses	81,058	48,907	32,505		32,505	24,136	20,867	45,003	48,353
Income (loss) before income taxes, unusual and extraordinary items	23,893	10,079	4,187		4,187	2,229	(10,222)	(7,993)	(13,972)
Net gain on sale of discontinued operations				\$ 4,795	4,795				
Income taxes	11,517	5,241	2,000	1,200	3,200				
Benefit of loss carry forward (3)	(11,369)	(5,241)	(2,000)	(1,200)	(3,200)				
Other extraordinary item									(14,800)
Net income (loss) (4)	\$23,745	\$10,079	\$4,187	\$ 4,795	\$ 8,982	\$2,229	\$(10,222)	\$(7,993)	\$(28,772)
Net income (loss) per Common Share (4) (5):									
Cdn. GAAP	\$0.93	\$0.50	\$0.28	\$0.31	\$0.59	\$0.10	\$(1.45)	\$(1.35)	\$(5.20)
U.S. GAAP	\$0.91	\$0.49	\$0.28	\$0.31	\$0.59	\$0.11	\$(1.45)	\$(1.34)	\$(2.70)



(000's)  
August 31

	1987	1986	1985	1984(1)	1983(1)
<b>Balance Sheet Data:</b>					
Working capital	\$141,348	\$ 68,918	\$ 8,397	\$(62)	\$ 4,687
Total assets	220,820	115,115	21,764	28,304	28,559
Capital lease obligations	3,554	682	1,623	2,120	3,146
Other long term debt		406		3,772	249
Shareholders' equity	172,732	86,898	12,272	429 (6)	8,351 (6)

(1) Includes discontinued Software Product Business. It is not practicable to segregate the results of operations of discontinued operations for 1983.

(2) The results of Capital Systems, Inc. are included from May 1, 1986 and the results of Yipkon Corporation are included from February 2, 1987. See note 2 of the Notes to the Consolidated Financial Statements for the 1987 fiscal year.

(3) Amounts charged to operations in fiscal 1982, 1983 and 1984 associated with product development, marketing and sales relating to the discontinued software product business contributed to losses of which approximately \$15 million are available at August 31, 1987 to the Company to reduce or eliminate income taxes otherwise payable on future earnings.

(4) Pursuant to Cdn. GAAP, the Company deferred and amortized certain software development costs until 1983. Under U.S. GAAP such amounts would have been expensed as incurred and, consequently, net loss in conformity with U.S. GAAP in

1983 was \$14,518,000. During fiscal 1983, there were no income tax recoveries or extraordinary items under U.S. GAAP.

(5) On a fully diluted basis for fiscal 1985. For all other years, the fully dilutive calculations would not be materially dilutive or would be antidilutive. All share and per share data included herein give effect to adjustments in share capital including a consolidation of Common Shares on a one-for-five basis effective January 31, 1985 and a two-for-one subdivision effective December 10, 1986. See note 6 of the Notes to the Consolidated Financial Statements for the 1987 fiscal year.

(6) Pursuant to U.S. GAAP, the Company's First Preference Shares, none of which is currently outstanding, would be considered to be redeemable preference shares and, as such, are to be presented outside Shareholders' Equity. The amounts of First Preference Shares outstanding at August 31, 1984 and 1983 were \$26,786,000 and \$26,903,000 respectively.



# Common Share Information

## Principal Markets

The NASDAQ National Market System is the principal market on which the Company's shares are traded. The shares are also traded on The Toronto Stock Exchange and The Montreal Exchange. The Company's shares were first listed on The Toronto Stock Exchange on August 25, 1980 and included on NASDAQ on June 14, 1985 and the National Market

System on November 5, 1985. The stock symbol of the Company's shares on NASDAQ is SHKIF and on The Toronto Stock Exchange and The Montreal Exchange it is SHK.

The following table sets forth the high and low prices for the Common Shares for the periods shown below.

### NASDAQ National Market System (U.S. Dollars)

	High	Low
<b>1985</b>		
Second Quarter (commencing June 14) _____	\$ 3.69	\$ 3.50
Third Quarter _____	3.88	3.25
Fourth Quarter October 1 — November 4, 1985 _____	3.32	3.32
November 5 — December 31, 1985 _____	5.07	3.38
<b>1986</b>		
First Quarter _____	6.25	4.75
Second Quarter _____	10.00	5.57
Third Quarter _____	9.88	7.57
Fourth Quarter _____	12.75	7.88
<b>1987</b>		
First Quarter _____	24.25	11.75
Second Quarter _____	22.63	17.88
Third Quarter _____	24.37	17.13

The NASDAQ quotations prior to November 5, 1985 are high and low bid prices and reflect inter-dealer prices, without retail mark-up, mark-down or commissions and may not necessarily represent actual transactions, and NASDAQ quotations after such date reflect high and low last sale prices.

### The Toronto Stock Exchange (Canadian Dollars)

	High	Low
<b>1984</b>		
First Quarter _____	\$ 4.35	\$ 2.75
Second Quarter _____	3.50	2.25
Third Quarter _____	2.50	1.63
Fourth Quarter _____	3.83	1.75
<b>1985</b>		
First Quarter _____	4.63	3.25
Second Quarter _____	5.19	3.50
Third Quarter _____	5.32	4.50
Fourth Quarter _____	6.82	4.38
<b>1986</b>		
First Quarter _____	8.69	6.63
Second Quarter _____	14.00	7.75
Third Quarter _____	13.82	10.50
Fourth Quarter _____	17.25	11.00
<b>1987</b>		
First Quarter _____	31.13	16.25
Second Quarter _____	30.00	24.00
Third Quarter _____	32.00	23.00

## Shareholders

As at October 16, 1987, there were approximately 1,400 shareholders of record.

## Dividends

The Company has not declared or paid any dividends on its Common Shares since February 1982 and the Board of Directors anticipates that all available funds will be applied in the foreseeable future to finance growth.

Under the Income Tax Act (Canada) (the "Act"), assuming that beneficial owners of the Common Shares are neither residents nor deemed to be residents of Canada and that they do not use or hold and are not deemed to use or hold the Common Shares in carrying on business in Canada, dividends paid by Systemhouse on its Common Shares will be subject to withholding tax at a maximum rate of 25% or such lower rate as may be provided for under the terms of an applicable bilateral tax treaty. Under the United States-Canada Tax Convention (1980), the rate of withholding tax on Systemhouse dividends paid or credited, or deemed paid or credited, to individuals residing in, or corporations organized under the laws

of, the United States, and not having a "permanent establishment" or "fixed base" in Canada, is reduced to 15%. The rate of withholding tax on dividends is further reduced under the Convention to 10% if the beneficial owner is a corporation resident in the United States and not having a "permanent establishment" or "fixed base" in Canada which owns at least 10% of the voting stock of Systemhouse.

On the basis of the assumptions set forth above, no other Canadian income or capital gains tax is payable under the Act by a non-resident of Canada in respect of the Common Shares or the dividends thereon, or any gains realized upon the disposition thereof, except on and to the extent of the capital gain realized on the disposition of Common Shares by a beneficial owner where such Common Shares are "taxable Canadian property" as defined by the Act. An applicable bilateral tax treaty may however, reduce or eliminate such tax, if it is exigible under the act.

## Exchange Rates of the Canadian Dollar

The high and low rates (i.e., the highest and lowest rates at which Canadian dollars were sold), the average exchange rate (i.e., the average of the exchange rates on the last day of each month during the period) and the period end exchange rate of the Canadian

dollar in exchange for U.S. currency for each of the five years ended December 31, 1986 and for the period January 1, 1987 through October 16, 1987, as reported by the Federal Reserve Bank of New York, were as follows:

	January 1 to October 16, 1987	1986	1985	1984	1983	1982
High	\$0.7701	\$0.7331	\$0.7575	\$0.8033	\$0.8201	\$0.8430
Low	0.7254	0.6954	0.7130	0.7492	0.7993	0.7691
Average	0.7536	0.7188	0.7308	0.7713	0.8108	0.8083
Period End	0.7701	0.7241	0.7151	0.7566	0.8035	0.8132



# Corporate Information

## Directors of the Company

Roderick M. Bryden  
Chairman & Chief Executive Officer  
SHL Systemhouse Inc.

Peter A. Sandiford  
President & Chief Operating Officer  
SHL Systemhouse Inc.

W. Alan Macfarlane  
Vice President, Finance & Secretary  
Kinburn Corporation  
*Investment Holding Company*

Charles E. O'Connor\*  
Chairman & Chief Executive Officer  
Kinburn Technology Corporation  
*Technology Management Company*

Dr. Michael C.J. Cowpland  
President, Corel Systems Corporation  
*Laser Publications Systems  
Manufacturer*

John C. Hardy\*  
President  
The Hendron Financial Group  
*Investment Holding Company*

Donald W. Paterson\*  
Vice President & Director  
Wood Gundy Inc.  
*Investment Dealer*

C. Ian Ross  
President  
Paperboard Industries Corporation  
*Paperboard & Corrugated Products  
Manufacturer*

\*Member of the Audit Committee

## Officers of the Company

Roderick M. Bryden  
Chairman & Chief Executive Officer

Peter A. Sandiford  
President & Chief Operating Officer

Stanley Udaskin  
Vice President, Finance and  
Administration

Jean-Pierre Soublière  
Executive Vice President  
Canadian Operations

Donald J. Lundgren  
Vice President & General Manager  
Ottawa Branch

Dennis B. Maloney  
Vice President & General Manager  
Toronto Branch

Robert B. Laurence  
Vice President & General Manager  
Federal Systems Branch

Andrew J. Bart  
Vice President & General Manager  
National Systems Branch

Howard G. Ulep  
Vice President  
Strategic Systems

W. Alan Macfarlane  
Secretary

Eileen Savoia  
Assistant Secretary



## **Auditors**

Clarkson Gordon  
Ottawa, Ontario

## **Legal Counsel (Canada)**

Gowling & Henderson  
Barristers & Solicitors  
Ottawa, Ontario

## **Legal Counsel (U.S.)**

Milbank, Tweed, Hadley & McCloy  
New York, New York

## **Stock Exchange Listings**

NASDAQ National Market System  
The Toronto Stock Exchange  
The Montreal Exchange

## **Transfer Agents & Registrars**

The Canada Trust Company  
Toronto, Ontario

The Chase Manhattan Bank, N.A.  
New York, New York

## **Bankers**

The Royal Bank of Canada

The Annual and Special Meeting of Shareholders of SHL Systemhouse Inc. will be held at 4:30 p.m., December 8, 1987, in the Confederation Ballroom, The Westin Hotel, 11 Colonel By Drive, Ottawa, Ontario, Canada.

A copy of the Company's Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission is available to shareholders without charge upon request to: Corporate Communications, SHL Systemhouse Inc., 50 O'Connor Street, 5th Floor, Ottawa, Ontario, Canada K1P 6L2.

Designed and produced by Wallace Kearney McGill  
Color separations by Chromascan  
Printed in Canada by Dollco Printing









