

RELIABILITY INC  
Form 10-Q/A  
May 19, 2003

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2003

Commission File Number 0-7092

RELIABILITY INCORPORATED

(Exact name of registrant as specified in its charter)

TEXAS

75-0868913

(State or other jurisdiction  
of incorporation or organization)

(I.R.S. Employer Identification Number)

16400 Park Row  
Post Office Box 218370  
Houston, Texas

77218-8370

(Address of principal executive offices)

(Zip Code)

(281) 492-0550  
(Registrant's telephone number, including area code)

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 twelve 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 ninety days.

YES

NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

6,335,965 -- Common Stock -- No Par Value  
as of May 12, 2003

RELIABILITY INCORPORATED  
FORM 10-Q

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The information furnished in this report reflects all adjustments (none of which were other than normal recurring accruals) which are, in the opinion of management, necessary to a fair statement of the results of the interim periods presented.

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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

RELIABILITY INCORPORATED  
CONSOLIDATED BALANCE SHEETS  
(In thousands, except share data)

## ASSETS

	March 31, <u>2003</u> (unaudited)	December 31, <u>2002</u> (Note 1)
Current assets:		
Cash and cash equivalents	\$ 5,447	\$ 6,117
Accounts receivable	304	296
Inventories	1,329	1,326
Refundable income taxes	3,751	3,677
Other current assets	<u>99</u>	<u>86</u>
 Total current assets	 <u>10,930</u>	 <u>11,502</u>
 Property, plant and equipment, at cost:		
Machinery and equipment	13,810	13,774

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Buildings and improvements	4,556	4,549
Land	<u>230</u>	<u>230</u>
	18,596	18,553
Less accumulated depreciation	<u>14,307</u>	<u>14,130</u>
	<u>4,289</u>	<u>4,423</u>
Investments	195	178
Assets held for sale	<u>1,285</u>	<u>2,005</u>
	\$16,699	\$18,108
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable	\$ 147	\$ 122
Accrued liabilities	593	652
Income taxes payable	27	29
Accrued restructuring costs	<u>77</u>	<u>92</u>
Total current liabilities	<u>844</u>	<u>895</u>

Deferred tax liabilities	133	53
--------------------------	-----	----

Stockholders' equity:

Common stock, without par value; 20,000,000 shares		
authorized; 6,690,265 shares issued	9,614	9,614
Retained earnings	7,218	8,668
Accumulated other comprehensive loss	(16)	(28)
Less treasury stock at cost, 354,300 shares in 2003 and 2002	<u>(1,094)</u>	<u>(1,094)</u>
	)	
Total stockholders' equity	<u>15,722</u>	<u>17,160</u>
	\$16,699	\$18,108
	=====	=====

See accompanying notes.

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RELIABILITY INCORPORATED  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(In thousands, except per share data)

	Three Months Ended March 31,	
	<u>2003</u>	<u>2002</u>
	(unaudited)	
Revenues:		
Product sales	\$ 205	\$ 830
Services	<u>223</u>	<u>404</u>
	<u>428</u>	<u>1,234</u>

Costs and expenses:

Cost of product sales	328	545
Cost of services	421	619
Marketing, general and administrative	829	1,012
Research and development	470	699
Asset impairment and restructuring costs	<u>—</u>	<u>323</u>
	<u>2,048</u>	<u>3,198</u>

Operating loss	(1,620)	(1,964)
Interest income	16	46
Gain on sale of building	<u>155</u>	<u>—</u>
Loss before income taxes	<u>(1,449)</u>	<u>(1,918)</u>

)

Provision (benefit) for income taxes:

Current	(74)	(268)
Deferred	<u>74</u>	<u>1</u>
	<u>—</u>	<u>(267)</u>

)

Net loss	<u><u>\$(1,449)</u></u>	<u><u>\$(1,651)</u></u>
----------	-------------------------	-------------------------

Loss per share:

Basic	\$ (.23)	\$ (.26)
	=====	=====
Diluted	\$ (.23)	\$ (.26)
	=====	=====
Weighted average shares:		
Basic	6,336	6,336
	=====	=====
Diluted	6,336	6,336
	=====	=====

See accompanying notes.

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RELIABILITY INCORPORATED  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)

	Three Months Ended March 31,	
	<u>2003</u>	<u>2002</u>
	(unaudited)	
Cash flows from operating activities:		
Net loss	\$ (1,449)	\$ (1,651)
Adjustments to reconcile net loss to cash used by operating activities:		
Depreciation and amortization	217	274
Provision for deferred income taxes	74	1
Provision for inventory obsolescence	15	9

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Provision for asset impairment and restructuring costs	-	323
Gain on disposal of fixed assets	(155)	-
Changes in operating assets and liabilities:		
Accounts receivable	(8)	(115)
Inventories	(18)	20
Refundable income taxes	(74)	(268)
Other current assets	(13)	68
Accounts payable	25	(6)
Accrued liabilities	(9)	1
Income taxes payable	(2)	6
Cash payments charged to restructuring reserve	<u>(15)</u>	<u>(156)</u>
	)	)
Total adjustments	<u>37</u>	<u>157</u>
Net cash used by operating activities	<u>(1,412)</u>	<u>(1,494)</u>
	)	)
Cash flows from investing activities:		
Expenditures for property and equipment	(83)	(163)
Proceeds from sale of assets held for sale	<u>825</u>	<u>-</u>
Net cash provided (used) by investing activities	<u>742</u>	<u>(163)</u>
	)	)
Cash flows from financing activities:		
Net cash provided (used) by financing activities	<u>-</u>	<u>-</u>



Effect of exchange rate changes on cash	—	(—2)
Net decrease in cash	(670)	(1,659)
Cash and cash equivalents:		
Beginning of period	<u>6,117</u>	<u>12,302</u>
End of period	\$5,447 =====	\$10,643 =====

See accompanying notes.

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RELIABILITY INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2003

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the interim period ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003.

The consolidated financial statements include the financial transactions and accounts of the Company and its wholly-owned subsidiary. All significant intercompany balances and transactions have been eliminated in consolidation.

The balance sheet at December 31, 2002 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2002.

## Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires that management make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

## Income Taxes

Deferred income taxes are provided under the liability method and reflect the net tax effects of temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements. The Company establishes valuation allowances when the realization of specific deferred tax assets are subject to significant uncertainty.

For the quarter ended March 31, 2003, the Company recorded no tax benefits on its operating loss, as the loss will have to be carried forward and realization of any benefit is uncertain. The offsetting current and deferred provision amounts result from additional deductions claimed on the Company's 2002 federal tax return which was filed during the quarter.

For the quarter ended March 31, 2002, U.S. losses were benefitted, as carryback benefits were available. No benefit was provided for foreign losses, thus the tax benefit rate was less than the U.S. statutory rate of 34%.

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RELIABILITY INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2003

## Inventories

Inventories are stated at the lower of standard cost (which approximates first-in, first-out) or market (replacement cost or net realizable value) and include (in thousands):

	March 31, <u>2003</u>	December 31, <u>2002</u>
Raw materials	\$ 493	\$ 501
Work-in-progress	578	538
Finished goods	<u>258</u>	<u>287</u>
	\$1,329 =====	\$1,326 =====

Inventories are presented net of reserves for excess and obsolete inventories of \$294,000 and \$280,000 at March 31, 2003 and December 31, 2002, respectively.

Investments in Marketable Equity and Debt Securities

All investments are classified as held to maturity or available-for-sale securities under the provisions of Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Management determines the appropriate classification of its investments in equity and debt securities at the time of purchase and reevaluates such determinations at each balance sheet date.

Marketable equity securities are classified as available-for-sale and are carried at their fair value on the balance sheet, with unrealized gains and losses, net of applicable income taxes of \$(8,000) and \$(14,000) at March 31, 2003 and December 31, 2002, respectively, reported as a separate component of stockholders' equity. Marketable equity securities are stated at market value, as determined by the most recently published trade price of the securities at the balance sheet date.

The following table summarizes the Company's investment in securities (in thousands) at the dates indicated:

	<u>March 31,</u> <u>2003</u>	<u>December 31,</u> <u>2002</u>
Marketable equity securities, at cost	\$219	\$219
Unrealized net losses on marketable securities		<u>(41</u>
	<u>(24)</u> )	
	\$195	\$178
Amount classified as current	<u>—</u>	<u>—</u>
Amount classified as long-term	\$195 <u>===</u>	\$178 <u>===</u>

## 2. SEGMENT INFORMATION

The following table presents reportable segment information (in thousands) for the periods indicated:

	Three Months Ended March 31,	
	<u>2003</u>	<u>2002</u>
Revenues from external customers:		
Testing Products	\$ 77	\$ 675
Services	223	404
Power Sources	128	155
Intersegment revenues:		
Testing Products	11	23
Services		-
Power Sources		-
Eliminations	<u>(11)</u>	<u>(23)</u>
	)	)
	\$ 428	\$1,234
	===	=====
Operating loss:		
Testing Products	\$ (909)	\$ (812)
Services	(273)	(375)
Power Sources	(275)	(358)
Asset impairment and restructuring costs of a Services operation	-	(323)
General corporate expenses	<u>(163)</u>	<u>(96)</u>
	)	

Operating loss	\$(1,620)	\$(1,964)
	=====	=====

Total assets by reportable segment as of the dates indicated are as follows (in thousands):

	March 31, <u>2003</u>	December 31, <u>2002</u>
Testing Products	\$ 4,705	\$ 5,434
Services	1,930	1,927
Power Sources	429	266
General corporate assets	<u>9,635</u>	<u>10,481</u>
	\$16,699	\$18,108
	=====	=====

For the periods indicated above, there were no material changes in the accounting policies and procedures used to determine segment income or loss.

RELIABILITY INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2003

3. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted loss per share (in thousands, except per share data):

	Three Months Ended March 31,
	<u>2003</u> <u>2002</u>

Net loss	\$(1,449)	\$(1,651)
	=====	=====
Weighted average shares outstanding	6,336	6,336
Net effect of dilutive stock options based on the treasury stock method	-----	-----
Weighted average shares and assumed conversions	6,336	6,336
	=====	=====
Income (loss) per share:		
Basic	\$ (.23)	\$ (.26)
	=====	=====
Diluted	\$ (.23)	\$ (.26)
	=====	=====

Options to purchase an average of 769,000 and 1,072,000 shares of common stock of the Company were excluded from the computation of the diluted loss income per share during the three months ended March 31, 2003 and 2002, respectively, as inclusion of these options in the calculations would have been anti-dilutive.

#### 4. COMPREHENSIVE LOSS

The only difference between the total comprehensive loss and the net loss reported on the Consolidated Statements of Operations arises from unrealized gains and losses on available-for-sale securities. The Company's total comprehensive loss (in thousands) for the periods indicated, is as follows:

	Three Months Ended March 31,	
	<u>2003</u>	<u>2002</u>
Net loss	\$(1,449)	\$(1,651)
Unrealized net gains (losses) on marketable equity securities	<u>12</u>	<u>(6)</u>

		)
Total comprehensive loss	\$(1,437)	\$(1,657)
	====	====

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RELIABILITY INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2003

**5. ASSET IMPAIRMENT AND RESTRUCTURING COSTS**

The following table reports activity in the accrued restructuring costs account during the three months ended March 31, 2003 (in thousands):

Accrued costs at January 1, 2003	\$ 92
Cash payments charged to accounts:	
Lease payments	<u>(15)</u>
	)
Accrued costs at March 31, 2003	\$ 77
	===

**6. SALE OF BUILDING**

On January 20, 2003 the Company completed the sale of the building formerly occupied by its Costa Rica subsidiary. Cash proceeds of \$825,000 were received, resulting in a gain of \$155,000.

## 7. STOCK OPTION PLAN

The Company has a stock option plan that provides for the grant of options to employees and directors of the Company. The term and vesting of each option is determined by the Board of Directors. The Company accounts for stock options using the intrinsic value based method prescribed by APB 25. Had the Company elected to account for stock options using the fair value method described in SFAS No. 123, the Company's reported net loss would have increased to the amounts shown below:

	Three Months Ended March 31,	
	<u>2003</u>	<u>2002</u>
Reported net loss	\$(1,449)	\$(1,651)
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards, net of related tax effects	<u>    (32)</u>	<u>    (84)</u>



Pro forma net loss	\$(1,481)	\$(1,735)
	=====	=====
Net loss per share, as reported:		
Basic	\$ (.23)	\$ (.26)
	=====	=====
Diluted	\$ (.23)	\$ (.26)
	=====	=====
Pro forma net loss per share, as if the fair value method had been applied to all awards:		
Basic	\$ (.23)	\$ (.27)
	=====	=====
Diluted	\$ (.23)	\$ (.27)
	=====	=====

The pro forma disclosures above are not necessarily indicative of the effects of applying SFAS 123 in future periods.

## 8. SUBSEQUENT EVENT - REDUCTION IN WORKFORCE

Due to a continued lack of demand for the Company's testing products and power sources, the Company reduced its Houston-based workforce by 25% in April 2003. Severance costs of \$234,000\_ were incurred and will be reported in the second fiscal quarter.

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

March 31, 2003

Item 2. Management's Discussion and Analysis of Financial Condition and Results of  
Operations

FORWARD-LOOKING STATEMENTS

This Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this document contain forward-looking statements that involve risks and uncertainties, as well as current expectations and assumptions. From time to time, the Company may publish forward-looking statements, including those that are contained in this report, relating to such matters as anticipated financial performance, business prospects, technological developments, new products, research and development activities and similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. In order to comply with the terms of the safe harbor, the Company notes that a variety of factors could cause the Company's actual results and experience to differ materially from the anticipated results or other expectations expressed in the Company's forward-looking statements. The risks and uncertainties that may affect the operations, performance, development and results of the Company's business include, but are not limited to, adverse changes in the global economy, sudden decreases in the demand for electronic products and semiconductors, market acceptance of the Company's products and services, the impact of competition, delays in product development schedules, delays due to technical difficulties related to developing and implementing technology, delays in delivery schedules, the ability to attract and maintain sufficient levels of people with specific technical talents, future results related to investments, and changes in demand for the Company's products and services and the Company's customers' products and services. All forward-looking statements included in this document are based on information available to the Company on the date hereof, and the Company assumes no obligation to update any such forward-looking statements.

#### CRITICAL ACCOUNTING POLICIES AND COMMENTS RELATED TO OPERATIONS

The Company has defined a critical accounting policy as one that is both important to the portrayal of the Company's financial condition and results of operations and requires the management of the Company to make difficult, subjective or complex judgments. Estimates and assumptions about future events and their effects cannot be perceived with certainty. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments. These estimates may change as new events occur, as more experience is acquired, as additional information is obtained and as the Company's operating environment changes. There have been no material changes or developments in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies and Estimates as disclosed in our Form 10-K for the year ended December 31, 2002.

The Management's Discussion included in the Form 10-K for the year ended December 31, 2002 includes discussion of various factors related to the decline in the Company's revenues and items related to the Company's results of operations, liquidity and markets. There have been no significant changes in most of the factors discussed in the Form 10-K and many of the items discussed in the Form 10-K are relevant to 2003 operations; thus the reader of this document should read the Management's Discussion included in Form 10-K for the year ended December 31, 2002.

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

March 31, 2003

#### LIQUIDITY AND CAPITAL RESOURCES

The primary sources of Reliability's liquidity have historically been cash provided by operations and working capital. As of March 31, 2003 the Company's working capital was \$10.1 million, of which \$5.4 million was cash and cash equivalents. Changes in the Company's financial condition and liquidity since December 31, 2002 are generally attributable to the net loss incurred in the quarter ended March 31, 2003.

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Certain ratios and amounts monitored by management in evaluating the Company's financial resources and performance are presented in the following chart. The periods presented that are related to profitability ratios are for the three months ended March 31, and twelve months ended December 31:

	March 31, 2003	December 31, 2002	March 31, 2002
Working capital:			
Working capital (in thousands)	\$10,086	\$10,607	\$12,354
Current ratio	13.0 to 1	12.9 to 1	11.8 to 1
Equity ratios:			
Total liabilities to equity	0.1	0.1	0.1
Assets to equity	1.1	1.1	1.1
Profitability ratios:			
Gross profit	(75)%	(8)%	6 %
Return on revenues	(339)%	(126)%	(134)%
Return on assets (annualized)	(35)%	(28)%	(30)%
Return on equity (annualized)	(37)%	(30)%	(32)%

Net cash used by operating activities for the three months ended March 31, 2003 was \$1.4 million, compared with \$1.5 million used by operations in the comparable quarter of 2002.

Net cash provided by investment activities during the first three months of 2003 was \$742,000 compared to \$163,000 used in investment activities during the comparable quarter of 2002. Net cash provided was primarily proceeds from the sale of the Company's property in Costa Rica.

During the recent and ongoing downturn of the semiconductor industry, the Company has sustained significant negative financial trends, including substantial decreases in revenues, net income, backlog, and cash flows from operating activities. Key customers have continued to delay or reduce expenditures for the Company's products and services. Management believes such trends may continue in the near term. Throughout this downturn, the Company has continued to restructure its operations and cost structure.

The Company's future strategy is primarily dependent on its ability to sell its newest generation of burn-in and test systems for medium and high power micrologic devices, the CRITERIA 20. As a result of the current and ongoing downturn of the semiconductor industry, target customers for the CRITERIA 20

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

March 31, 2003

have continued to delay capital expenditures for new capacity, and no sales have been made to date. While management believes that the first sales of the CRITERIA 20 will occur in late 2003, no assurances can be made that market demand will return or that market acceptance can be achieved in that time frame.

Considering the results of management's recent cost-cutting and restructuring actions, the Company's limited financial obligations, its current cash balances, and expected proceeds from the tax refund expected in the second quarter of 2003, management believes that it has sufficient cash to meet its working capital and capital equipment needs through fiscal 2003 and into 2004. Depending on the Company's growth, profitability and other factors, including market conditions, the Company may require additional capital resources after fiscal 2003. There can be no assurances that additional financing will be available when required or that such financing can be obtained on terms satisfactory to the Company.

## RESULTS OF OPERATIONS

Three months ended March 31, 2003 compared to three months ended March 31, 2002.

### Revenues.

Revenues in the first quarter of 2003, while 65% lower than the first quarter of 2002, were only 6% lower than the fourth quarter of 2002. Revenues in the Testing Products and Power Sources segments were down sequentially, while revenues in the Testing Services segment increased by \$44,000, or 25% over the previous quarter.

### Costs and Expenses

. Total costs and expenses in the first quarter of 2003 decreased by \$1,150,000 from the comparable quarter in 2002 and by \$881,000 from the fourth quarter of 2002. Excluding provisions for asset impairment, restructuring and severance, the decrease from the first and fourth quarters of 2002 were \$827,000 and \$190,000, respectively. Expense reductions are largely the result of cost controls and restructuring actions taken by management to improve the Company's cost structure in response to the continuing economic slowdown.

Additionally, the Company reduced its Houston-based workforce by 25% in April 2003. Severance costs of \$234,000 were incurred and will be reported in the second fiscal quarter.

### Income Taxes

. No tax benefit was recorded on the operating loss incurred in the quarter ended March 31, 2003, as no carryback benefits were available and realization of tax benefits in future periods is uncertain. In the prior year, the Company was able to offset its taxable loss against taxes paid in prior years and file a refund claim.

Item 3. Quantitative and Qualitative Disclosure of Market Risk.

There have been no material changes in the market risk disclosures reported in the Company's Annual Report on Form 10-K filed for the year ended December 31, 2002.

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

March 31, 2003

Item 4. Controls and Procedures.

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Acting Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-5 under the Securities Exchange Act. Based on that evaluation, the Company's Chief Executive Officer and Acting Chief Financial Officer had concluded that the Company's disclosure controls and procedures are effective.

There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation described in the preceding paragraph.

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RELIABILITY INCORPORATED  
OTHER INFORMATION

**PART II - OTHER INFORMATION**

March 31, 2003

Items 1 through 4 are not applicable and have been omitted.

Item 5. Other information.

On April 1, 2003, the Company received a letter from the Nasdaq Stock Market regarding noncompliance with the qualification standards for continued listing of its common stock on the Nasdaq National Market, as a result of the closing bid price of the Company's common stock being less than \$1.00 for 30 consecutive business days. The Company will have 180 calendar days, or until September 29, 2003 to regain compliance. If at anytime before September 29, 2003, the bid price of the Company's common stock closes at \$1.00 per share or more for a minimum of 10 and up to 20 consecutive trading days the Company will have achieved compliance with this qualification standard. If compliance cannot be demonstrated by September 29, 2003 the Company may appeal to a Listing Qualifications Panel or may apply to transfer its common stock to the Nasdaq SmallCap Market.

On April 16, 2003, the Company received an additional letter from the Nasdaq Stock Market regarding noncompliance with the qualification standards for continued listing of its common stock on the Nasdaq National Market as a result of the market value of the Company's publicly held shares being less than \$5,000,000 for the last 30 consecutive trading days. The Company will have 90 calendar days, or until July 15, 2003, to regain compliance. If at anytime before July 15, 2003, the market value of the Company's publicly held shares is \$5,000,000 or greater for a minimum of 10 consecutive trading days, the Company will have regained compliance with this qualification

standard. If compliance cannot be demonstrated by July 15, 2003 the Company may appeal to a Listing Qualifications Panel or may apply to transfer its common stock to the Nasdaq SmallCap Market.

Item 6. Exhibits and Reports on Form 8-K:

(a) The following exhibits are filed as part of this report:

- |      |                                                                                                                        |
|------|------------------------------------------------------------------------------------------------------------------------|
| 99.1 | Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of The Sarbanes-Oxley Act Of 2002 |
| 99.2 | Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of The Sarbanes-Oxley Act Of 2002 |

(b) Reports on form 8-K.

Current report on Form 8-K filed on February 12, 2003, pursuant to Item 12.

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RELIABILITY INCORPORATED  
SIGNATURES

March 31, 2003

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

RELIABILITY INCORPORATED  
(Registrant)

May 12, 2003

Larry Edwards

Larry Edwards  
President and Chief Executive Officer

May 12, 2003

James M. Harwell

James M. Harwell  
Acting Chief Financial Officer

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CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Larry Edwards, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Reliability Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under



which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the "Evaluation Date"); and
  - c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this report whether there were

significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ Larry Edwards  
Larry Edwards  
Chief Executive Officer  
May 12, 2003

CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, James Harwell, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Reliability Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the "Evaluation Date"); and
  - c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ James Harwell  
James Harwell  
Acting Chief Financial Officer  
May 12, 2003