2012 ANNUAL REPORT

MOVING FORWARD

Depicted on the cover is a progression through the Company's history including our early years' central stations and equipment; Philip Kleinman (CEO from 1968-1995); current day central station and latest technological user applications offered by the Company.

Originally founded in 1873, AFA has provided uninterrupted central station alarm service to its customers for almost 140 years.

Corporate Profile

AFA's Central Station service consists of a detecting system installed in subscribers' premises and frequently owned, serviced, monitored, inspected and maintained by AFA. The vast majority of signals from subscribers' premises are transmitted to AFA's Central Stations via subscribers' telephone lines, GSM cellular networks or over the Internet. AFA presently operates redundant UL Listed and FM Approved state-of-the-art computerized Central Stations servicing the United States. Our Central Stations operate twenty-four hours a day, seven days a week and monitor approximately 38,000 AFA subscriber locations. The Company also monitors approximately 12,000 locations for customers of approximately 150 Alarm Dealers who do not have their own central stations. Upon receipt of an alarm signal, AFA personnel take the appropriate action, which may include alerting Fire or Police Departments, verifying an alarm condition, notifying its subscribers, and dispatching AFA personnel or other response agents to the protected premises.

The Primary Scope of AFA's Services Includes:

- Fire detection systems;
- Burglar and vandalism protection;
- Monitoring of subscriber-owned systems;
- Access control systems;
- Smoke detection;
- Installation, maintenance and testing of high-rise life safety systems;
- Sprinkler alarm supervision;
- Closed circuit TV (CCTV) systems;
- Remote video surveillance;
- Video verification of alarm;
- Industrial process supervision, including temperature;
- Sump pump and air conditioning supervision;
- Flood detection;
- Boiler supervision;
- Remote access to and control of alarm system;
- Investigator response.

The majority of the Company's revenues come from the sale and installation of specialized alarm systems including sophisticated high-rise fire and life safety systems which the Company designs and installs to meet proliferating fire and life safety codes. The Company is also a provider of video surveillance systems and intrusion related services whereby customers can remotely view and control their own systems.

AFA does not manufacture detecting equipment. Technology continues to change rapidly and new equipment is so readily available that AFA can better meet subscribers' needs by selecting quality products available from the industry's top suppliers.

AFA's core revenues include the recurring annual service fees paid by customers for Central Station monitoring, inspection and maintenance services.

Letter To Our Shareholders

As expected, in 2012 the Company's performance was noticeably better than during the prior two years. The organizational changes management implemented during 2011-2012 made a positive impact. With staffing now more commensurate with our level of business and the significant cost burdens of health care and auto maintenance being brought under relative control, the foundation was laid for the Company to post better financial results. Moreover, the difficult conversion of our accounting and operational software systems was virtually completed early in the year, thereby relieving a great deal of burden on many in the Company and allowing them to focus more on the fundamentals of the business itself. All this, coupled with what appeared to be a better economic environment, led to the Company posting improved results in almost every category.

Net income in 2012 amounted to $2,253,000 or $14.74 per share as compared to $1,348,000 or $8.79 per share in 2011. Cash flow from operating activities in 2012 amounted to $2,739,000 or $17.92 per share as compared to $1,761,000 or $11.49 in 2011. Overall revenues rose from year to year: $73,870,000 in 2012 as compared to $71,520,000 in 2011.

For the first time in five years, the Company experienced year to year increases in booked sales and backlog. New booked sales in 2012 amounted to $36,383,000, an increase of 7% over 2011. At year end, our backlog had grown by 6% to $12,639,000. Ironically, the one metric where the Company did not perform quite as well as the year before was its gross attrition rate, which rose to 7.8%. This slight uptick was the direct result of one significant loss. Still, on balance, the Company's performance in retaining business was close to our target and far superior to the industry norm. These factors led once again to the Company's ability to organically grow its recurring revenue base for the fourteenth consecutive year.

Last year the Company also returned to the acquisition market. Freed up from the internal diversions of the previous two years, the Company was able to refocus on some tabled projects and consummate the purchase of two companies during 2012. These acquisitions added $1 million to the Company's annual recurring revenues. The first acquisition, Sera Security Systems, marked the Company's return to the Philadelphia marketplace. This addition was also significant as it bolstered our presence in the Southern New Jersey area, provided a seasoned and experienced workforce, and filled a void in our National Accounts operational capacity. At the end of the year, the Company acquired United Telephone Services, Inc., including its wholly owned subsidiary Ready Alarm, a provider of commercial central station fire alarm services in New York City with a solid customer base in the real estate industry. Both of these acquisitions have been fully integrated into our operation smoothly and notably with virtually no attrition. The combination of these acquisitions and the aforementioned organic recurring revenue growth resulted in an overall year end gain to the Company's recurring revenue base of 5%.

Unlike the Company as a whole, our National Accounts Division experienced a 9% reduction in booked sales as compared to the prior year. This was due entirely to a 25% reduction in sales to the Division's principal account. During the year, the Division was able to offset much of this reduction by setting records for sales to other accounts (up 60% as compared to the prior year) and in recurring revenues (double that of any prior year). In doing so, the Division added five new accounts and continued to expand the scope of services being rendered to existing accounts. This momentum has continued into early 2013, which to date is on pace to surpass 2012 sales production.

The flagship New York Branch was expected to do well in 2012 and did so, with a solid year across the board. By year end, the branch had posted 5% gains in new booked sales, operating profits, ending recurring revenues, and year-end backlog as compared with 2011. The branch also managed to contain its attrition at an excellent gross rate of 5%.

The New England branch had a mediocre year. While it managed to achieve slightly improved earnings and maintain its recurring revenue base, it experienced reductions in new sales and backlog. Having already experienced some recurring revenue losses in 2013, management is currently analyzing this branch to determine why it has underperformed recently in comparison to our other established branches.

Our New Jersey branch continued its resurgence from last year, with 12% increases in new sales and year-end backlog. Earnings from the branch were consistent with the prior year's results.

Aided in large part by the further development of accounts added in recent years' acquisitions, the Georgia branch's revenue base continued to expand in 2012. The end result was a 27% increase in sales including a significant increase in the sales of new recurring revenues. The year-end backlog also increased by 20%.

Our Midlantic branch continued to improve, most notably with its 28% increase in new sales. This was particularly significant in that the increase was generated from the branch itself rather than from National Accounts referrals.

The North Carolina branch experienced a slight setback, caused by a significant reduction in work referred from our National Accounts Division. Although its results were below expectations, the branch is no longer the cash drain that it was years ago and is still positioned to be a contributor to the Company's bottom line going forward.

By the second quarter of 2012, the wholesale changes made in the Florida branch served to stop that branch's bleeding of cash. The slimmed-down branch has settled down and is now showing signs of possibly entering into a growth mode later this year. Based on past experience however, management will be cautious before authorizing any significant expansion of current financial support in this region without commensurate booked sales.

Overall, we entered 2013 stronger than a year ago. As alluded to earlier, our employees are no longer distracted with the process of implementing the software conversions and are focused on improving the Company's financial, sales and operational capabilities. During 2012 we began to embrace the modern age of marketing by utilizing the Internet, our vendors, and other mass marketing techniques to reach new potential subscribers. We have implemented a tracking system to follow these efforts; and I can report that even though the Company is in its infancy with this approach, we have already seen tangible results over the past few months in the form of new sales.

The Company has always been on the cutting edge in providing its services. In 1873 the Company offered the first fire alarm detection systems in the country. In 1970 the Company developed and marketed the first usable Multiplex transmission system in the industry. We are continuing to embrace the latest industry technology to enable us to keep at the forefront of all of the services we have traditionally sold, as well as to embark on selling different, but related products and services. For example, in 2012 the Company introduced "AFA Vision," a new generation alarm system enabling our customers to remotely access their systems and control the system from a smart phone or computer. Providing our customers with these new offerings demonstrates that the Company is constantly moving forward, as it has done throughout its 140 year history.

At the end of 2012, your Board of Directors, confident in our direction going forward and mindful of impending changes in the country's tax laws, declared a special dividend of $6 per share and advanced all of the 2013 regular dividends into 2012. Given the totality of the circumstances last December, the Board unanimously believed these actions were in the shareholders' best interests. At the same time the Board voted to expand and added two new members: David Kleinman and Thomas Von Essen. Mr. Kleinman is a Vice President of the Company and is involved with supervising the Company's operations as well as performing various legal functions for the Company. Mr. Von Essen is currently an independent consultant in the fire safety industry and is internationally known for his earlier service as the New York City Fire Commissioner and his stewardship of the City's Fire Department in the wake of 9/11. His intimate knowledge of the fire industry should be particularly well suited to advise and assist the Company, which still relies on that arena for a significant portion of its business.

Looking ahead, we expect our performance in 2013 to surpass that achieved in 2012, with increases in both new sales, revenues and earnings.

Robert D. Kleinman
Chairman and Chief Executive Officer

AFA Protective Systems, Inc. and Subsidiaries

Consolidated Balance Sheets

December 31,	2012	2011
Assets		
Current assets		
Cash and cash equivalents	**$ 1,356,329**	$ 1,768,982
Accounts receivable, net of allowance for doubtful accounts	**13,600,216**	14,641,524
Inventories	**4,656,379**	4,179,938
Prepaid expenses and other current assets	**573,106**	549,429
Total current assets	**20,186,030**	21,139,873
Property, plant and equipment, net	**7,447,871**	8,478,768
Goodwill and intangible assets, net	**7,363,741**	464,290
Other assets	**160,253**	265,916
Total assets	**$35,157,895**	$30,348,847
Liabilities and Shareholders' Equity		
Current liabilities		
Current portion of long-term debt	**$ 4,790,821**	$ 2,373,786
Accounts payable	**4,006,106**	4,547,308
Accrued expenses and other current liabilities	**4,084,806**	4,515,140
Deferred revenues	**5,975,659**	5,995,079
Total current liabilities	**18,857,392**	17,431,313
Long-term debt	**4,530,619**	5,921,445
Deferred income taxes	**2,090,052**	–
Pension obligation	**2,018,905**	2,495,668
Obligation for postretirement benefits	**246,964**	260,950
Deferred revenues	**1,572,963**	1,846,609
Fair value of interest rate swaps	**319,515**	423,298
Total liabilities	**29,636,410**	28,379,283
Commitments and Contingencies (Note 16)		
Shareholders' equity		
Common stock, $1 par value; 1,500,000 shares authorized; 163,080 shares issued and outstanding in 2012 and 153,278 in 2011	**163,080**	153,278
Additional paid-in capital	**3,057,694**	316,142
Accumulated other comprehensive loss	**(1,968,710)**	(2,228,903)
Retained earnings	**4,269,421**	3,729,047
Total shareholders' equity	**5,521,485**	1,969,564
Total liabilities & shareholders' equity	**$35,157,895**	$30,348,847

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

AFA Protective Systems, Inc. and Subsidiaries

Consolidated Statements of Income and Comprehensive Income

Years Ended December 31,	2012	2011
Revenues		
Sales	$42,644,275	$41,393,367
Service	31,225,229	30,126,903
	73,869,504	71,520,270
Costs and expenses		
Cost of sales	31,564,504	30,841,018
Cost of services, exclusive of depreciation and amortization	18,802,430	19,347,949
Depreciation and amortization	1,991,035	1,943,107
Selling, general, and administrative	17,345,577	16,755,815
	69,703,546	68,887,889
Income from operations	4,165,958	2,632,381
Interest and dividend income	19,882	74,882
Interest expense, net	(283,766)	(382,761)
Income before provision for income taxes	3,902,074	2,324,502
Provision for income taxes	1,649,000	977,000
Net income	$ 2,253,074	$ 1,347,502
Earnings per share	$ 14.74	$ 8.79
Weighted average number of shares outstanding	152,832	153,278
Dividends per share	$ 10.00	$ 2.00
Comprehensive income		
Net income	$ 2,253,074	$ 1,347,502
Net actuarial gain (loss) arising during the year, net of taxes	245,882	(520,138)
Interest rate swap, net of taxes	14,311	(54,856)
Comprehensive income	$ 2,513,267	$ 772,508

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

AFA Protective Systems, Inc. and Subsidiaries

Consolidated Statements of Shareholders' Equity

Years Ended December 31, 2012 and 2011

	Number of Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Total
Balance at December 31, 2010	153,278	$ 153,278	$ 316,142	$ (1,653,909)	$ 2,688,101	$ 1,503,612
Net income for the year	–	–	–	–	1,347,502	1,347,502
Cash dividends ($2.00 per share)	–	–	–	–	(306,556)	(306,556)
Net actuarial loss arising during the year	–	–	–	(520,138)	–	(520,138)
Interest rate swap	–	–	–	(54,856)	–	(54,856)
Balance at December 31, 2011	153,278	$ 153,278	$ 316,142	$ (2,228,903)	$ 3,729,047	$ 1,969,564
Net income for the year	–	–	–	–	**2,253,074**	**2,253,074**
Cash dividends ($10.00 per share)	–	–	–	–	**(1,525,741)**	**(1,525,741)**
Purchase & retirement of common stock	**(748)**	**(748)**	**(1,448)**	–	**(186,959)**	**(189,155)**
Shares issued to purchase United Telephone Services, Inc.	**10,550**	**10,550**	**2,743,000**	–	–	**2,753,550**
Net actuarial gain arising during the year	–	–	–	**245,882**	–	**245,882**
Interest rate swap	–	–	–	**14,311**	–	**14,311**
Balance at December 31, 2012	**163,080**	**$163,080**	**$3,057,694**	**$(1,968,710)**	**$4,269,421**	**$5,521,485**

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

AFA Protective Systems, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31,	2012	2011
Cash flows from operating activities		
Net income	$ 2,253,074	$ 1,347,502
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	1,991,035	1,924,850
Deferred income taxes	64,700	311,300
(Gain) loss on interest rate swap	(79,908)	3,177
Changes in operating assets and liabilities		
Accounts receivable	1,066,487	(2,384,975)
Inventories	(476,441)	115,240
Prepaid expenses and other current assets	(23,677)	319,353
Other assets	(18,894)	(17,355)
Accounts payable	(1,053,612)	1,673,517
Accrued expensesand other current liabilities	(505,537)	(1,167,606)
Deferred revenues	(397,216)	(410,262)
Liability for postretirement benefits	(80,867)	46,071
Net cash provided by operating activities	2,739,144	1,760,812
Cash flows from investing activities		
Capital expenditures	(802,742)	(1,714,274)
Acquisition of assets	(1,660,369)	–
Net cash used in investing activities	(2,463,111)	(1,714,274)
Cash flows from financing activities		
Dividends paid	(1,525,741)	(306,556)
Purchase and retirement of common stock	(189,155)	–
Proceeds from borrowings–line of credit	3,900,000	1,000,000
Repayments of line of credit	(1,500,000)	–
Repayments of mortgage note	(273,790)	(257,753)
Repayments of term loan	(1,100,000)	(1,100,000)
Net cash used in financing activities	(688,686)	(664,309)
Net decrease in cash and cash equivalents	(412,653)	(617,771)
Cash and cash equivalents		
Beginning	1,768,982	2,386,753
Ending	$ 1,356,329	$ 1,768,982
Supplemental disclosures of cash flow information		
Cash paid for:		
Interest	$ 334,086	$ 383,104
Income taxes	1,543,144	325,903
Non-cash investing activities (Note 2)		
Assets acquired from United Telephone Services, Inc., net	2,753,550	

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

1. Organization and Basis of Presentation

Description of the Business

AFA Protective Systems, Inc. and Subsidiaries (the "Company") is engaged in the installation, operation, maintenance and sale of protective systems to safeguard life and property from a variety of hazards. Operations are conducted primarily in the eastern United States.

Basis of Presentation

The financial statements include the accounts of AFA Protective Systems, Inc. and its subsidiaries, all of which are wholly owned. All intercompany balances and transactions have been eliminated in consolidation.

2. Summary of Significant Accounting Policies

Revenue Recognition

Service charges to alarm system subscribers, for services to be rendered over a maximum period of one year, are deferred and taken into income as earned over the service period. Advance service billings on new subscribers are also deferred and reflected in income over a five-year period, the term of most contracts. For income tax purposes, the Company reports advance billings as income in the year billed. Selling expenses in connection with obtaining new subscribers are charged to income from operations as incurred.

The percentage-of-completion method is used for the recognition of revenue from sales of security systems under long-term contracts in accordance with ASC 605-35, "Revenue Recognition–Construction Type and Production Type Contracts," and is based on the ratio of costs incurred to date on the contract to total estimated contract costs, after providing currently for all known or anticipated losses. Due to uncertainties inherent in the estimation process, it is possible that completion costs will be revised in the near term. Such revisions to costs and income are recognized in the period in which the revisions are determined.

Fair Value of Financial Instruments

In assessing the fair value of financial instruments at December 31, 2012 and 2011, the Company has used a variety of methods and assumptions, which were based on estimates of market conditions and risks existing at the time. The fair value of financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, approximate their carrying value because of the current nature of these instruments. The carrying value of the Company's long-term borrowings at December 31, 2012 and 2011 approximate fair value as interest rates approximate current market rates based on their variable nature. The Company believes its mortgage interest rate reflects current market rates. The Company's interest rate swaps have been measured at fair value under the same principles.

Cash and Cash Equivalents

Cash and cash equivalents include short-term investments with original maturities of 90 days or less. At December 31, 2012 and 2011, cash and cash equivalents included money market funds of $90,800 and $90,600, respectively. Cash and cash equivalents held at financial institutions may at times exceed federally insured amounts. The Company believes it mitigates its risks by investing in or through major financial institutions.

Accounts Receivable

Accounts receivable are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a regular basis. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history and current economic conditions. Accounts receivable are written off when deemed uncollectible. Recoveries of accounts receivable previously written off are recorded when received.

Inventories

Inventories consist of finished goods, work in progress and parts which are carried at the lower of cost (on a first-in, first-out basis) or market. The Company continues to evaluate the inventories on a periodic basis for slow moving, excess and obsolete stock on hand.

Property, Plant and Equipment

Property, plant and equipment are recorded at their historical cost and depreciated over their estimated useful lives, which range from 3 to 30 years. Maintenance and repairs are charges to expense as incurred; renewals and improvements that extend the life of the asset are capitalized. Upon retirement or sale, the asset cost and related accumulated depreciation are eliminated from the respective accounts and the resulting gains or loss, if any, is included in the results of operations for the year. Leasehold improvements are amortized over the shorter of the lease term or remaining useful life of the related assets.

Central station equipment, equipment in subscribers' premises and other equipment are depreciated primarily by accelerated methods. The straight-line method is used for buildings and leasehold improvements. For income tax purposes, installation costs are deducted as incurred and accelerated methods and rates are used for all other assets.

Debt Issue Costs

Debt issue costs are being amortized using the interest method over the term of the related debt. Amortization of $18,257 has been recorded in amortization expense in the consolidated statements of income and comprehensive income in each of the years ended December 31, 2012 and 2011.

Goodwill and Intangible Assets

Goodwill and indefinite lived intangible assets are not amortized but instead are reviewed annually for impairment or more frequently if impairment indicators arise. The Company tests for impairment whenever events or changes in circumstances indicate that the carrying amount of goodwill or other intangible assets may not be recoverable or at least annually at December 31 of each year. In the event that the Company determines that the value of goodwill or other intangible assets have become impaired, the Company will incur a charge for the amount of the impairment during the fiscal period in which the determination is made. The Company completed its review and determined there was no impairment during the years ended December 31, 2012 and 2011 (Note 5). Identifiable intangible assets represent primarily alarm contracts arising from acquisitions and are amortized on a straight-line basis over their estimated useful lives ranging primarily from four to eight years.

Impairment of Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate the carrying value of the assets may not be recoverable. In reviewing for impairment, the Company compares the carrying value of the assets to the estimated undiscounted future cash flows expected from the use of the assets and their eventual disposition. When the estimated undiscounted future cash flows are less than their carrying amount, an impairment loss is recognized equal to the difference between the assets' fair value and its carrying amount. The Company believes the future cash flows to be received from its long-lived assets exceed the assets' carrying value, and accordingly, the Company has not recognized any impairment losses for the years ended December 31, 2012 and 2011.

Concentration of Credit Risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, are primarily trade accounts receivable. Customers in the commercial real estate industry, principally commercial building properties, account for a substantial portion of trade receivables. Credit risk with respect to trade receivables is generally minimized due to the large corporations and other organizations the Company services. Accounts receivable due from a major customer amounted to approximately $2,468,000 and $3,064,000 at December 31, 2012 and 2011, respectively. Billings to this customer amounted to $14,555,000 and $17,421,000 for the years ended December 31, 2012 and 2011, respectively.

Advertising Costs

Costs for advertising are expensed when incurred. Advertising expense was approximately $150,000 and $153,000 for the years ended December 31, 2012 and 2011, respectively.

Earnings per Share

Earnings per share is computed by dividing net income by the weighted average number of shares outstanding during the reporting period. The Company has no dilutive securities.

Income Taxes

Deferred income taxes are provided for the tax effects of differences between the financial reporting and tax bases of the Company's assets and liabilities at the enacted tax rates in effect for the years in which the differences are expected to reverse. The Company evaluates the recoverability of deferred tax assets and establishes a valuation allowance when it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Company recognizes tax liabilities when, despite the Company's belief that its tax return positions are supportable, the Company believes that certain positions may not be fully sustained upon review by tax authorities. Benefits from tax positions are measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon settlement. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences impact income tax expense in the period in which such determination is made. Interest and penalties, if any, related to accrued liabilities for tax positions are included in interest expense.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include accounting for long-term contracts, the allowance for doubtful accounts, inventory obsolescence, depreciation and amortization, employee benefit plans, income taxes and contingencies.

Derivative Financial Instruments

The Company accounts for derivative instruments in accordance with ASC 815, "Derivatives and Hedging." ASC 815 requires that the Company recognize all derivatives as assets or liabilities and measure those instruments at fair value. The Company uses derivatives primarily for the purpose of hedging exposure to changes in interest rates. The Company recognized a gain on an interest rate swap that does not qualify for hedge accounting of $80,000 for the year ended December 31, 2012 and a loss of $3,176 for the years ended December 31, 2011. The Company recorded a liability in connection with another interest rate swap that qualifies for hedge accounting of $67,545 and $91,456 for the years ended December 31, 2012 and 2011, respectively. The change in fair value has been included as a component of comprehensive income.

Comprehensive Income

Comprehensive Income consists of net income and other comprehensive income or loss. Other Comprehensive Income or loss consists of the net unrealized actuarial gains or losses related to the Company's postretirement and pension plans, and the fair value of its interest rate swap related to its term loan, net of income taxes.

Subsequent Events

The Company evaluated all events or transactions that occurred after the balance sheet date of December 31, 2012 through April 9, 2013, the date it issued these financial statements. Any subsequent events that required recognition or disclosure have been reflected in these financial statements.

Acquisitions

In 2012, the Company acquired certain assets, primarily customer alarm monitoring contracts, of SERA Security Services, Inc. for $1,660,369 funded principally through its unsecured line of credit with its primary bank.

In December 2012, the Company acquired United Telephone Services, Inc. ("United") in a tax-free transaction for a net distribution of 10,550 shares of AFA common stock with a value of $2,753,550. The purchase price was allocated primarily to contract intangibles of $5,300,000, net of deferred taxes. None of the intangibles related to the United acquisition are deductible for tax purposes. Intangibles and the corresponding deferred tax liability recorded are being amortized over 15 years.

3. ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

December 31,	**2012**	2011
Trade receivables, including progress bills and amounts due on completed contracts	**$11,786,511**	$13,183,600
Costs and estimated earnings in excess of billings on uncompleted contracts	**1,963,705**	1,607,924
	13,750,216	14,791,524
Less: allowance for doubtful accounts	**(150,000)**	(150,000)
	$13,600,216	$14,641,524

Cost and estimated earnings on uncompleted contracts and related amounts billed were as follows:

December 31,	**2012**	2011
Costs incurred on uncompleted contracts	**$ 3,737,577**	$ 3,886,530
Estimated earnings	**1,152,938**	1,441,845
	4,890,515	5,328,375
Less: billings to date	**(3,178,823)**	(4,019,751)
	1,711,692	1,308,624
Costs and estimated earnings in excess of billings (included in accounts receivable)	**(1,963,705)**	(1,607,924)
Billings in excess of costs (included in accrued expenses and other current liabilities)	**$ (252,013)**	$ (299,300)

Costs and estimated earnings in excess of billings on uncompleted contracts arise in the consolidated balance sheets when revenues have been recognized but the amounts cannot be billed under the terms of the contracts. Such amounts are recoverable from customers based upon various measures of performance, including achievement of certain milestones or completion of the contract. Substantially all amounts recorded as costs and estimated earnings in excess of billings on uncompleted contracts at December 31, 2012, are expected to be billed and collected within one year.

4. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment, net consists of the following:

	Estimated Lives	December 31, 2012	December 31, 2011
Land		**$ 242,000**	$ 242,000
Buildings	30	**4,679,235**	4,679,235
Equipment in subscribers' premises	10-25	**47,945,854**	47,114,631
Central station and other equipment	3-10	**17,077,430**	16,853,783
Leasehold improvements	Lesser of lease term or useful life	**380,121**	380,121
Installations in progress	*	**197,473**	449,601
		70,522,113	69,719,371
Less: accumulated depreciation		**(63,074,242)**	(61,240,603)
		$ 7,447,871	$ 8,478,768

*Depreciation expense is initiated once equipment is fully installed and operational.

Depreciation expense was $1,833,639 and $1,908,071 for the years ended December 31, 2012 and 2011, respectively.

5. Goodwill and Intangible Assets, Net

Goodwill and intangible assets, net consists of the following:

	Estimated Lives	December 31, 2012	December 31, 2011
Goodwill	–	**$ 441,301**	$ 441,301
Alarm contracts and contract intangibles	4-15 years	**7,005,057**	199,365
Non compete and other agreements	5 years	**86,845**	–
Gross goodwill and intangibles		**7,533,203**	640,666
Less: accumulated amortization		**(169,462)**	(176,376)
Goodwill and intangible assets, net		**$7,363,741**	$ 464,290

Amortization of intangible assets was $139,139 and $16,779 during the years ended December 31, 2012 and 2011, respectively. Future estimated amortization expense for the next five years is as follows as of December 31, 2012:

Years ending December 31,	
2013	$ 452,988
2014	452,547
2015	450,295
2016	447,121
2017	436,819
	$2,239,770

6. Other Assets

Other assets consist of the following:

December 31,	2012	2011
Debt issue costs, net (Note 2)	**$ 47,320**	$ 65,577
Other	**112,933**	200,339
	$160,253	$265,916

7. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

December 31,	2012	2011
Salaries, wages and vacation	**$2,179,598**	$2,317,367
Employee benefit plan contribution	**141,231**	148,436
Current portion of liability for postretirement benefits	**43,900**	43,400
Income taxes payable	**44,506**	7,344
Billings in excess of costs	**189,914**	299,300
Healthcare costs payable	**500,000**	600,000
Refundable NYC Fire Department fees	**372,746**	611,716
Other	**612,911**	487,577
	$4,084,806	$4,515,140

8. Long-Term Debt

Long-term debt consists of the following:

December 31,	2012	2011
Line of credit	**$ 3,400,000**	$ 1,000,000
Term loan	**3,208,323**	4,308,333
Mortgage note	**2,713,117**	2,986,898
	9,321,440	8,295,231
Less: current portion	**(4,790,821)**	(2,373,786)
Long-term debt	**$ 4,530,619**	$ 5,921,445

Future maturities of long-term debt are as follows:

Years ending December 31,	
2013	$4,790,817
2014	1,408,906
2015	3,121,717
	$9,321,440

On June 1, 2005, the Company obtained a $4,400,000 ten-year mortgage from its primary bank collateralized by three buildings owned by the Company whose carrying value at December 31, 2012 and 2011 was approximately $1,252,000 and $1,408,000, respectively. Repayment is to be made in equal monthly installments of $37,249 based on an amortization schedule of fifteen years with interest of LIBOR (0.21% at December 31, 2012) plus 1.52%. The remaining principal balance of $1,924,393 will be due in full on July 15, 2015.

On December 1, 2010, the Company obtained a $5,500,000 five-year term loan from its primary bank collateralized by a blanket U.C.C. filing against its assets. Repayment is to be made in monthly principal installments of $91,667 with an interest rate of LIBOR plus 1.75%. The terms of the agreement contain various restrictive covenants which include, but are not limited to, maintenance of certain income to debt service ratios and certain adjusted earnings requirements, as defined.

In connection with the mortgage loan, the Company entered into an interest rate swap agreement, (the "Swap"), with its primary bank to effectively fix its variable interest rate at 6.05%. The fair value of the Swap of $(251,970) and $(331,842) at December 31, 2012 and 2011, respectively, has been recorded based on current market rates. This swap is not treated as a hedge. The Company has a swap on its five-year term loan with its lender to effectively fix its interest rate on the related debt at 3.44%. Such swap will be treated as a hedge. The fair value of the hedge totaling $(67,545) and $(91,456) at December 31, 2012 and 2011, respectively, has been recorded based on current market rates. The gain of $23,000, net of determined income taxes has been recognized in accumulated other comprehensive loss at December 31, 2012.

The Company has available $3,600,000 in a line of credit with its primary bank collateralized by a blanket U.C.C. filing against its assets expiring July 31, 2013. Interest is payable at LIBOR plus 2.10%. Use of the funds are unrestricted. As of December 31, 2012, the Company has outstanding advances of $3,400,000 against its line of credit, leaving $200,000 available for use.

9. Deferred Revenues

Deferred revenues consist of annual service and other charges and advance service charges. Annual service and other charges represent customer billings for services not yet rendered for which the maximum billing period is one year and have been reflected as a current liability. Advance service charges consist of nonrefundable charges billed to customers at the time of new installations. The portion of these charges expected to be recognized within one year has been classified as current on the balance sheet at December 31, 2012 and 2011. An analysis of deferred revenues is as follows:

	Annual Service and Other Charges	Advance Service Charges	Total
Balance at December 31, 2010	$ 4,722,843	$ 3,529,107	$ 8,251,950
Billings	28,809,998	906,643	29,716,641
Amortizations to income	(28,733,762)	(1,393,141)	(30,126,903)
Balance at December 31, 2011	4,799,079	3,042,609	7,841,688
Billings	**30,053,208**	**878,955**	**30,932,163**
Amortizations to income	**(29,949,628)**	**(1,275,601)**	**(31,225,229)**
Balance at December 31, 2012	**$ 4,902,659**	**$ 2,645,963**	**$ 7,548,622**

10. Common Stock

Issuance of Employee Stock Appreciation Rights

The Company issued stock appreciation rights to certain employees in January 2007 which will be payable only upon sale of the Company or change in its control, as defined. Since the sale of the Company or change in its control, as defined, are contingent events, no compensation expense is recorded until such events are probable of occurrence.

11. Income Taxes

Components of the provision for income taxes are as follows:

December 31,	2012	2011
Current		
Federal	**$1,233,187**	$509,005
State and local	**351,113**	156,695
	1,584,300	665,700
Deferred		
Federal	**23,600**	285,200
State and local	**41,100**	26,100
	64,700	311,300
	$1,649,000	$977,000

A reconciliation of the federal statutory rate and the Company's effective tax rate follows:

	2012	2011
Federal statutory rate	**34.0%**	34.0%
State and local income taxes, net of federal income tax benefit	**6.3%**	5.9%
Other items	**1.9%**	2.1%
Effective rate	**42.2%**	42.0%

The effective tax rate differed from the federal statutory tax rate primarily as a result of state income taxes and certain non-deductible expenses.

The tax effects of the significant temporary differences which comprise the deferred tax assets and liabilities at December 31 are as follows:

December 31,	2012	2011
Deferred Tax Assets		
Advance service revenue	**$ 1,181,300**	$ 1,349,800
Intangibles	–	238,300
Net operating loss carryforwards (state)	–	6,000
Benefit plans	**929,600**	1,092,900
Other	**228,700**	256,100
	2,339,600	2,943,100
Less: valuation allowance	–	(6,000)
Deferred tax assets	**2,339,600**	2,937,100
Deferred Tax Liabilities		
Intangibles	**(1,811,853)**	–
Depreciation	**(2,562,000)**	(2,789,700)
Other	**(55,799)**	(41,100)
Net deferred tax (liabilities) assets	**$(2,090,052)**	$ 106,300

As of December 31, 2012 and 2011, the Company recorded a valuation allowance of $0 and $6,000, respectively, on the deferred tax assets to reduce the total to an amount that management believes will ultimately be realized. Realization of deferred tax assets is dependent upon sufficient future taxable income during the period that deductible temporary differences and carryforwards are expected to be available to reduce taxable income. The net change in the valuation allowance against deferred tax assets were a decrease of $6,000 and $12,000 during the years ended December 31, 2012 and 2011, respectively. Net deferred tax assets at December 31, 2011 are included in other assets, as the current portion is not deemed significant.

Liabilities for uncertain tax positions reflected as of December 31, 2012 are not significant and it is not anticipated that they will materially change in the next 12 months. With limited exceptions, the Company is no longer subjected to tax audits by taxing authorities for years through 2008 for all jurisdictions. Although the outcome of tax audits is always uncertain, the Company believes that its tax positions will generally be sustained under audit.

Interest expense and penalties related to income tax matters are recognized as a component of interest expense. For the years ended December 31, 2012 and 2011, the Company did not record any liabilities or expenses related to tax penalties and related interest.

12. Retirement Benefits

The Company maintains a noncontributory defined benefit pension plan for its hourly union employees who meet certain requirements of age, length of service and hours worked per year. The benefits provided are based upon years of service and the employee's compensation during the last five years of employment. The Company's funding policy is to contribute annually at least the minimum amount required by Federal regulations. Effective October 15, 1996, the collective bargaining agreement covering the New York/New Jersey union employees was terminated following a strike, which resulted in a workforce reduction. Accordingly, the plan was amended effective December 31, 1996, to eliminate benefit accruals for the remaining New York/New Jersey employees. Effective January 1, 1997, the plan was further amended to provide those participants whose benefits were frozen due to the termination of the union agreement, to have their benefits determined using the method applicable for early retirement if they continue in service until then. In conjunction with the Company's collective bargaining agreement effective August 1, 2007 covering its Massachusetts union employees effective February 1, 2008, the plan was amended to eliminate benefit accruals for the Massachusetts employees, and new employees are no longer eligible to enter the plan.

The Company provides certain health care and life insurance benefits to retired employees who have attained age 62 or 20 years of service at the date of retirement, whichever is later. Eligible retirees under age 65 are covered by the Company's health

insurance plan, at a cost to the retiree equal to the Company's cost for an active employee. After attaining age 65, an eligible retiree's health care benefit coverage becomes coordinated with Medicare, with the retiree paying a portion of the cost of the coverage in excess of certain amounts. Effective December 31, 1996, the Company eliminated future benefits for employees who had not already retired or had given notice of retirement at that date. The Company's funding policy is generally to pay covered expenses as they are incurred.

The following is a reconciliation of the benefit obligation, fair value of plan assets and funded status of the Company's defined benefit and other postretirement benefit plans measured at December 31, 2012 and 2011, respectively:

	Pension Benefits		Other Postretirement Benefits	
	2012	2011	**2012**	2011
Change in Benefit Obligation				
Benefit obligation at beginning of year	**$ 7,991,099**	$ 6,697,425	**$ 304,350**	$ 340,345
Service cost	**—**	—	**—**	—
Interest cost	**307,179**	356,404	**9,778**	13,030
Actuarial (gain) loss	**(149,303)**	1,209,175	**28,548**	(6,684)
Benefits paid	**(261,217)**	(271,905)	**(51,812)**	(42,341)
Benefit obligation at end of year	**$ 7,887,758**	$ 7,991,099	**$ 290,864**	$ 304,350
Change in Plan Assets				
Fair value of plan assets at beginning of year	**$ 5,495,431**	$ 5,146,860	**$ —**	$ —
Actual return on plan assets	**402,589**	502,476	**—**	—
Employer contribution	**232,000**	118,000	**51,812**	42,341
Benefits paid	**(261,217)**	(271,905)	**(51,812)**	(42,341)
Fair value of plan assets at end of year	**$ 5,868,803**	$ 5,495,431	**$ —**	$ —
Benefit obligations in excess of fair value	**$(2,018,955)**	$(2,495,668)	**$(290,864)**	$(304,350)

Amounts recognized in the consolidated balance sheet consist of:

	Pension Benefits		Other Postretirement Benefits	
	2012	2011	**2012**	2011
Non-current pension liability	**$(2,018,905)**	$(2,495,668)	**$ —**	$ —
Current portion of liability for postretirement benefits	**—**	—	**(43,900)**	(43,400)
Non-current liability for postretirement benefits	**—**	—	**(246,964)**	(260,950)
Net amount recognized	**$(2,018,905)**	$(2,495,668)	**$(290,864)**	$(304,350)

Amounts recognized in accumulated other comprehensive loss consist of:

	Pension Benefits		Other Postretirement Benefits	
	2012	2011	**2012**	2011
Actuarial loss	**$2,988,651**	$3,403,209	**$225,114**	$220,438
Total	**$2,988,651**	$3,403,209	**$225,114**	$220,438

The amounts shown above have been recognized in accumulated other comprehensive loss totaling $1,928,165, net of deferred income tax assets of $1,285,700, at December 31, 2012 and accumulated other comprehensive loss totaling $2,174,047, net of deferred income tax assets of $1,449,600, at December 31, 2011.

Amounts recorded in other comprehensive loss consist of:

	Pension Benefits			Other Postretirement Benefits		
	2012			**2012**		
	Before Tax Amount	Tax (Expense) or Benefit	Net of Tax Amount	Before Tax Amount	Tax (Expense) or Benefit	Net of Tax Amount
Net actuarial (gain) loss arising during the year	**$(254,093)**	**$(101,600)**	**$(152,493)**	**$28,548**	**$11,400**	**$17,148**
Less: amortization included in net periodic pension cost	**160,464**	**64,200**	**96,264**	**23,873**	**9,600**	**14,273**
Net change during the year	**$(414,557)**	**$(165,800)**	**$(248,757)**	**$ 4,675**	**$ 1,800**	**$ 2,875**

Components of net periodic pension and other postretirement benefits cost:

	Pension Benefits		Other Postretirement Benefits	
	2012	2011	**2012**	2011
Interest cost	**$ 307,179**	$ 356,404	**$ 9,778**	$13,030
Expected return on plan assets	**(297,850)**	(328,773)	**—**	—
Amortization of net losses	**160,464**	138,225	**23,873**	23,626
Total	**$ 169,793**	$ 165,856	**$33,651**	$36,656

Amounts recorded in accumulated other comprehensive loss expected to be recognized as a component of net periodic pension cost in 2013 are as follows:

	Pension Benefits	Other Postretirement Benefits
Actuarial loss	$162,281	$24,180
Total	$162,281	$24,180

Weighted average assumptions used to determine the benefit obligation and net periodic pension and other postretirement benefits cost as of and for the years ended December 31:

	Pension Benefits		Other Postretirement Benefits	
	2012	2011	**2012**	2011
Discount rate used for net periodic cost	**4.16%**	5.27%	**3.38%**	4.40%
Discount rate used for benefit obligation	**3.82%**	4.16%	**2.83%**	3.38%
Expected return on plan assets	**5.40%**	6.50%	**—**	—

The expected return on plan assets has been determined based on historical rates of return.

The assumed increase in health care cost trend rate at the end of 2012 was 8%, gradually decreasing to 5% by the year 2015 and is expected to remain at that level thereafter. A one percentage point increase or decrease in these trend rates would not have a significant effect on the accumulated benefit obligation at December 31, 2012 and the net periodic pension and other postretirement benefits cost for 2012.

Plan Assets

Assets are primarily invested in the General Account of Principal Mutual Life Insurance Company, which provides the contract and cashout value of the account. The Company's defined benefit plan investment strategy is to invest the assets in a conservative portfolio that provides an acceptable return with low down-side risk. Preservation of capital is of primary importance. The funds are invested principally in guaranteed investment contracts which are reinvested in new contracts upon expiration. The General Investment Account is a low-risk fixed income investment, consistent with the defined benefit plan's strategy. The breakdown of the cashout value of the assets as of December 31, 2012 and 2011 is as follows:

	2012	2011
General Investment Account	**95.3%**	95.9%
Principal Financial Group Stock Separate Account	**4.7%**	4.1%

Cash Flows

Benefit payments, which reflect expected future service, as appropriate, expected to be paid for the next ten years are as follows:

Years ending December 31,	Pension Benefits	Other Postretirement Benefits
2013	$ 347,300	$ 43,900
2014	364,200	37,100
2015	380,800	31,800
2016	401,700	27,700
2017	421,100	24,400
2018-2021	2,202,800	89,500
	$4,117,900	$254,400

Substantially all non-union salaried employees of the Company were covered by another defined contribution pension plan. Contributions under the plan were based on specified percentages of the compensation of covered employees less forfeitures, if any. There is no unfunded past service cost for this plan. In January 2010, the Company terminated the plan and offered its employees covered by this plan to fully participate in the Company's 401(k) Plan discussed in the following paragraph. Pension expense for this plan was $0 for the years ended December 31, 2012 and 2011, respectively.

In connection with the aforementioned curtailment of the defined benefit pension plan, effective December 1, 1996 and the curtailment of the defined contribution plan discussed above, the Company established a 401(k) savings plan covering all eligible employees. Under the plan, employees may contribute up to certain percentages of their pretax earnings, subject to the Internal Revenue Service annual contribution limit. The Company can make non-matching and matching contributions for all eligible employees. Company contributions to the plan amounted to approximately $471,000 and $474,000 for the years ended December 31, 2012 and 2011, respectively.

13. Related Party Transactions

In 1968, the Company entered into an agreement with Ready Alarm, Inc. ("Ready") which provides for the sale to Ready of alarm systems installed prior to November 1, 1967 in the premises of a substantial portion of the Company's subscribers. In 1970, Ready was acquired by United Telephone Services, Inc. ("United"), all of the outstanding shares of which are owned by the Chairman of the Company, members of his family and family trusts. There have been no sales of alarm systems to Ready since its acquisition by United in 1970.

Pursuant to a United shareholders' agreement, all shares of the Company owned by United and present shareholders of United, which represent approximately 54% of the outstanding shares of the Company, are voted as directed by the Chairman.

The Company received approximately $142,000 and $134,000 in 2012 and 2011, respectively, for central station protection services rendered to Ready's subscribers. As discussed in Note 2, the Company purchased the stock of United and its Ready Alarm subsidiary on December 31, 2012.

14. Fair Value of Financial Instruments

The Company measures fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering assumptions, generally accepted accounting principles establishes a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date:

- *Level* 1—Observable inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;
- *Level* 2—Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the same term of the financial instrument; and
- *Level* 3—Unobservable inputs to the valuation methodology in which there is little or no market data and which are significant to the fair value measurement.

The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the

lowest level input that is significant to the fair value measurement of the instrument.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and counterparty creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company's valuation methodologies may produce a fair value calculation that may not be indicative of net realized value or reflective of future values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Cash equivalents consisting of money market funds are reported at fair value utilizing Level 1 Inputs. Derivatives are reported at fair value utilizing Level 2 Inputs. The Company obtained dealer quotations to assist it in the valuation of its interest rate swaps.

December 31, 2012	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Cash equivalents	**$90,800**	**$ –**	**$ –**	**$ 90,800**
Derivative liabilities	**–**	**319,515**	**–**	**319,515**

December 31, 2011	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Cash equivalents	$90,600	$ –	$ –	$ 90,600
Derivative liabilities	–	423,298	–	423,298

15. New York City Fire Department Litigation

In June 2008, the Company reached a settlement in an ongoing action against the New York City Fire Department. All disputed fees had been paid into an independent escrow fund pending resolution of the matter. The Company received approximately $3,860,000 of which approximately $2,559,000 was retained by the Company as a reimbursement of costs incurred since 1994, with the balance of approximately $1,301,000 to be returned to the Company's customers in the form of credits against future Fire Department fees. The Company has recorded a liability of $373,000 and $612,000 at December 31, 2012 and 2011, respectively, in connection with credits issuable to its customers related to this matter.

16. Commitments and Contingencies

Leases

The Company is obligated under the terms of noncancellable operating leases for office, storage and operating facilities (real property) through 2017 for approximate aggregate minimum rentals of $3,108,000 as follows:

Years ending December 31,	
2013	$1,039,000
2014	951,000
2015	725,000
2016	326,000
2017	67,000
	$3,108,000

Certain leases are renewable and substantially all leases provide for payment of various cost escalations. Rent expense for all operating leases, including motor vehicles, was approximately $2,254,000 and $2,137,000 for the years ended December 31, 2012 and 2011, respectively.

Other

Various claims incident to the ordinary course of business, some of which have resulted in litigation, are pending against the Company. In the opinion of management, disposition of these matters will not have a material adverse effect on its consolidated financial position, results of operations or cash flows.

Report of Independent Auditors

To the Board of Directors and Shareholders of
AFA Protective Systems, Inc:

We have audited the accompanying consolidated financial statements of AFA Protective Systems, Inc. and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

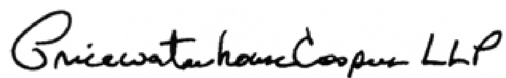
Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal controls. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of AFA Protective Systems, Inc. and its subsidiaries at December 31, 2012 and 2011, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



April 9, 2013
Melville, New York

AFA Protective Systems, Inc. and Subsidiaries

Selected Financial Data

For Each of the Five Years in the Period Ended December 31, 2012.

	2012	2011	2010	2009	2008
Sales	**$42,644,275**	$41,393,367	$42,443,870	$48,023,623	$52,683,340
Service revenues	**$31,225,229**	$30,126,903	$29,989,431	$30,049,342	$29,123,167
Net income	**$ 2,253,074**	$ 1,347,502	$ 997,350	$ 2,155,019	$ 2,577,452
Earnings per share	**$ 14.74**	$ 8.79	$ 6.51	$ 14.05	$ 16.80
Cash dividends per share	**$ 10.00**(a)	$ 2.00	$ 52.00(b)	$ 2.00	$ 22.00(c)
Average number of shares outstanding	**152,832**	153,278	153,278	153,388	153,435
At year end:					
Deferred revenues	**$ 7,548,622**	$ 7,841,688	$ 8,251,950	$ 9,551,039	$ 9,380,806
Property, plant and equipment, net	**$ 7,447,871**	$ 8,478,768	$ 8,672,565	$ 9,557,013	$10,096,607
Total assets	**$35,157,895**	$30,348,847	$29,137,357	$32,678,126	$33,485,536
Shareholders' equity	**$ 5,521,485**(a)	$ 1,969,564	$ 1,503,612(b)	$ 8,762,346	$ 7,515,736(c)
Number of shares outstanding	**163,080**	153,278	153,278	153,278	153,420
Book value per share	**$ 33.86**(a)	$ 12.85	$ 9.81(b)	$ 57.17	$ 48.99(c)

(a) The Board of Directors approved a special dividend of $6.00 per share and advanced its 2013 dividend of $2.00 per share to shareholders of record on December 14, 2012.
(b) The Board of Directors approved a special dividend of $50 per share to shareholders of record on December 1, 2010 and paid on December 15, 2010.
(c) The Board of Directors approved a special dividend of $20 per share to shareholders of record on September 15, 2008 and paid on October 15, 2008.

AFA Protective Systems, Inc. and Subsidiaries

Market Prices and Dividend Information

The Company's Common Stock is traded in the over-the-counter market. The range of high and low bid quotations as provided by the National Association of Security Dealers qualified interdealer quotation medium and the amount of cash dividends paid per share for each of the quarters of the fiscal years ended December 31, 2012 and 2011 are as follows:

Year Ended December 31, 2012			
Quarter		Bid	Dividends
1	High	**$242**	**$ .50**
	Low	**240**	
2	High	**253**	**.50**
	Low	**242**	
3	High	**260**	**.50**
	Low	**248**	
4	High	**257**	**8.50**
	Low	**255**	
			$10.00

Year Ended December 31, 2011			
Quarter		Bid	Dividends
1	High	$250	$ .50
	Low	240	
2	High	244	.50
	Low	237	
3	High	244	.50
	Low	237	
4	High	238	.50
	Low	236	
			$2.00

AFA Protective Systems, Inc. and Subsidiaries

Executive and Regional Offices

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Corporate Information

Board of Directors

Asher Bernstein
President, Bernstein Management Corp., a real estate company, New York, NY

Stephen Hess*
President, Hess Associates, Manhasset, NY

Stephen Genatt*
President, Genatt Associates, New Hyde Park, NY

David M. Kleinman
Vice President and Secretary, AFA Protective Systems, Inc.

Richard D. Kleinman
President, AFA Protective Systems, Inc.

Robert D. Kleinman
Chairman of the Executive Committee and Board of Directors, AFA Protective Systems, Inc.

Fredric Mack
Partner, The Mack Company Fort Lee, NJ

Thomas Von Essen
Fire and Life Safety Consultant Former Commissioner– City of New York Fire Department

*Members of Audit Committee

Officers

Robert D. Kleinman
Chairman of the Board of Directors, Chief Executive Officer and General Counsel

Richard D. Kleinman
President and Chief Operating Officer

Raymond S. Greenberger
Vice President and Chief Financial Officer, Treasurer and Assistant Secretary

Stephen P. Hyle
Vice President and Director of National Accounts

David M. Kleinman
Vice President and Secretary

Registrar and Transfer Agent

Registrar and Transfer Company
10 Commerce Drive
Cranford, NJ 07016

Independent Auditors

PricewaterhouseCoopers LLP
401 Broad Hollow Road
Melville, NY 11747

Annual Meeting

The Annual Meeting of Stockholders will be held on Wednesday, May 29 at 11:30 a.m. at the Company's Corporate Headquarters, 155 Michael Drive, Syosset, New York. All stockholders are invited to attend. A formal Notice of Meeting accompanies this report.

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