

# Quadlogic Controls Corporation

Financial Statements  
Years Ended February 28, 2019 and 2018

# Quadlogic Controls Corporation

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Financial Statements  
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# Quadlogic Controls Corporation

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## Independent Auditor's Report

The Board of Directors  
Quadlogic Controls Corporation  
Long Island City, New York

We have audited the accompanying financial statements of Quadlogic Controls Corporation, which comprise the balance sheets as of February 28, 2019 and 2018, and the related statements of income, changes in shareholders' equity (deficit) and cash flows for the years then ended, and the related notes to the financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of 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 these 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 entity's internal control. 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Quadlogic Controls Corporation as of February 28, 2019 and 2018, and the results of its operations and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

BDO USA, LLP

June 27, 2019

# Quadlogic Controls Corporation

## Balance Sheets

<i>February 28,</i>	2019	2018
<b>Assets</b>		
<b>Current Assets</b>		
Cash	\$ 97,342	\$ 128,094
Accounts receivable, trade, net of allowance for doubtful accounts of \$64,298 and \$73,437 in 2019 and 2018	2,775,077	1,754,430
Inventories, net	1,008,890	1,361,031
Prepaid expenses and other current assets	191,756	170,311
<b>Total Current Assets</b>	<b>4,073,065</b>	<b>3,413,866</b>
<b>Property and Equipment, Net</b>	<b>814,672</b>	<b>648,650</b>
<b>Other Assets</b>		
Other assets	-	388,915
Patent and trademark costs, net of accumulated amortization of \$170,828 in 2019 and \$142,964 in 2018	369,635	385,616
Lease deposits	191,854	191,854
<b>Total Other Assets</b>	<b>561,489</b>	<b>966,385</b>
<b>Total Assets</b>	<b>\$ 5,449,226</b>	<b>\$ 5,028,901</b>
<b>Liabilities and Shareholders' Equity (Deficit)</b>		
<b>Current Liabilities</b>		
Current maturities of installment debt	\$ 376,852	\$ 118,467
Current maturities of capital lease obligations	23,448	-
Accounts payable	1,969,676	1,418,533
Customer deposits	78,000	102,809
Accrued compensation	485,321	559,236
Accrued expenses and other liabilities	685,115	779,673
<b>Total Current Liabilities</b>	<b>3,618,412</b>	<b>2,978,718</b>
<b>Non-Current Liabilities</b>		
Installment debt, net of current maturities	-	376,852
Capital lease obligations, net of current maturities	97,591	-
Secured line of credit - borrowings	1,102,234	938,275
Other non-current liabilities	561,285	801,836
<b>Total Non-Current Liabilities</b>	<b>1,761,110</b>	<b>2,116,963</b>
<b>Total Liabilities</b>	<b>5,379,522</b>	<b>5,095,681</b>
<b>Commitments</b>		
<b>Shareholders' Equity (Deficit)</b>		
Common stock - \$0.001 par value; 20,000,000 shares authorized, and 11,638,351 and 11,373,351 shares issued and outstanding as of February 28, 2019 and 2018, respectively	11,638	11,373
Additional paid-in capital	9,582,434	9,499,549
Accumulated deficit	(9,524,368)	(9,577,702)
<b>Total Shareholders' Equity (Deficit)</b>	<b>69,704</b>	<b>(66,780)</b>
<b>Total Liabilities and Shareholders' Equity (Deficit)</b>	<b>\$ 5,449,226</b>	<b>\$ 5,028,901</b>

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Statements of Income

<i>Year ended February 28,</i>	2019	2018
<b>Revenues</b>		
Meter sales	\$ 8,204,674	\$ 7,259,784
Royalty income	-	1,000,000
Billing and technical services	6,249,277	5,542,408
<b>Total Revenues</b>	<b>14,453,951</b>	<b>13,802,192</b>
<b>Cost of Goods Sold</b>		
Cost of meters sold	5,615,046	4,854,540
Cost of billing and technical services	3,198,150	2,969,308
<b>Total Cost of Goods Sold</b>	<b>8,813,196</b>	<b>7,823,848</b>
<b>Gross Profit</b>	<b>5,640,755</b>	<b>5,978,344</b>
<b>Operating Expenses</b>		
Selling	1,500,430	1,598,198
Research and development	1,127,740	1,319,852
General and administrative	2,750,858	2,878,891
<b>Total Operating Expenses</b>	<b>5,379,028</b>	<b>5,796,941</b>
<b>Operating Income</b>	<b>261,727</b>	<b>181,403</b>
<b>Other Expense</b>		
Interest expense	(179,370)	(143,249)
Other expense, net	(29,023)	(30,989)
<b>Total Other Expense</b>	<b>(208,393)</b>	<b>(174,238)</b>
<b>Net Income</b>	<b>\$ 53,334</b>	<b>\$ 7,165</b>

*See accompanying notes to financial statements.*

**Quadlogic Controls Corporation**  
**Statements of Changes in Shareholders' Equity (Deficit)**

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*Years ended February 28, 2019 and 2018*

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total
	Number of Shares	Par Value			
<b>Balance, February 28, 2017</b>	11,373,351	\$ 11,373	\$ 9,499,549	\$ (9,584,867)	\$ (73,945)
Net income	-	-	-	7,165	7,165
<b>Balance, February 28, 2018</b>	11,373,351	11,373	9,499,549	(9,577,702)	(66,780)
Issuance of common stock to directors	215,000	215	67,935	-	68,150
Vesting of restricted common stock to employees	50,000	50	14,950	-	15,000
Net income	-	-	-	53,334	53,334
<b>Balance, February 28, 2019</b>	11,638,351	\$ 11,638	\$ 9,582,434	\$ (9,524,368)	\$ 69,704

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Statements of Cash Flows

<i>Year ended February 28,</i>	2019	2018
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 53,334	\$ 7,165
Adjustment to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	225,186	212,700
Provision for doubtful accounts	1,388	3,780
Stock-based compensation	83,150	-
Write-off patents	-	36,957
Loss on abandoned equipment	-	35,300
Changes in assets and liabilities:		
Accounts receivable	(1,022,035)	259,902
Inventories	741,056	167,035
Prepaid expenses and other current assets	(21,445)	24,934
Accounts payable	391,143	(407,152)
Customer deposits	(24,809)	(87,124)
Accrued expenses and other liabilities	(94,558)	(231,593)
Accrued compensation	(73,915)	(96,552)
Other non-current liabilities	(240,551)	(181,717)
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>17,944</b>	<b>(256,365)</b>
<b>Cash Flows from Investing Activities</b>		
Purchase of property and equipment	(69,552)	(27,300)
Patent acquisition costs	(11,882)	(15,246)
<b>Net Cash Used in Investing Activities</b>	<b>(81,434)</b>	<b>(42,546)</b>
<b>Cash Flows from Financing Activities</b>		
Principal debt repayments	(131,221)	(28,431)
Borrowing from line of credit	14,004,379	14,335,000
Repayments of line of credit	(13,840,420)	(14,007,647)
<b>Net Cash Provided by Financing Activities</b>	<b>32,738</b>	<b>298,922</b>
<b>Net (Decrease) Increase in Cash</b>	<b>(30,752)</b>	<b>11</b>
<b>Cash, beginning of year</b>	<b>128,094</b>	<b>128,083</b>
<b>Cash, end of year</b>	<b>\$ 97,342</b>	<b>\$ 128,094</b>
<b>Supplemental Disclosure of Cash Flow Information</b>		
Interest paid	\$ 176,331	\$ 112,793
<b>Supplemental Disclosures of Noncash Investing and Financing Activities</b>		
Prepaid insurance financed by installment notes	\$ 47,834	\$ 43,301
Acquisition of third-party software under financing arrangement	160,000	-
Acquisition of property and equipment under capital lease	133,793	-

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 1. Summary of Significant Accounting Policies

This summary of the significant accounting policies of Quadlogic Controls Corporation (Quadlogic, or the Company) is presented to assist in the understanding of the financial statements. The financial statements and notes are representations of the Company's management, which is responsible for the integrity and objectivity of the financial statements. These accounting policies conform to U.S. generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

#### *History and Business Activity*

The Company is engaged in the business of electricity metering. The business consists of two groups: The Systems Group, designing, manufacturing and selling "smart" metering systems, digital electricity meters and associated equipment that measure and remotely monitor the time and amount of electricity consumption, and perform other diagnostics. While most Quadlogic meters feature the Company's proprietary robust power line communications technology, increasingly, the Company is joining the "IoT" world (Internet of Things) with products like its new Qlic™ eMeter, that employ other communications modalities and become part of a multi-utility data and communication hub. The Services Group consists of technical services including meter reading, customer billing, and system repair and maintenance. In prior years, the Company also generated revenue from the licensing of certain intellectual property associated with their Energy Guard product. Currently there are no active licensing arrangements as of February 28, 2019.

The Company's revenues for the fiscal years ended February 28, 2019 and 2018 included sales to foreign customers of 30.6% and 29.4%, respectively. Canadian sales represented approximately 26.4% and 29.2% and other foreign sales represented 4.2% and 0.2% of total revenues for the fiscal years ended February 28, 2019 and 2018, respectively. In addition, the Company had recorded royalty income from Mexico of \$0 and \$1,000,000 for the years February 28, 2019 and 2018, respectively. The Company's customers include real estate development and construction companies, owners and operators of multi-tenant commercial and residential buildings, distributors, foreign electric utility companies and licensees.

The Company's stock is not listed on any organized exchange but is traded on the over-the-counter market. The Company's common stock is quoted on the OTC Markets (Pink) and experiences limited trading activity.

#### *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 and liabilities, and the 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 could differ from those estimates.

#### *Accounts Receivable*

The Company carries its accounts receivable at cost less allowances for doubtful accounts and returns. On a periodic basis, the Company evaluates its accounts receivable and establishes allowances for doubtful accounts and returns based on a history of past write-offs, collections, returns and current conditions.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### *Revenue Recognition*

The Company recognizes revenue from the sale of electric metering equipment at the time of shipment to the customer. Revenues from meter read and bill services, and from repair and technical services, are recognized at the time the services are rendered. The Company has entered into certain arrangements with a customer to license technology. The customer is obligated to pay royalties to the Company when the product is shipped to the end user.

### *Fair Value of Financial Instruments*

The Company follows the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, "Fair Value Measurement," which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs).

The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under ASC 820 are described as follows:

*Level 1* - These are unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date.

*Level 2* - These are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

*Level 3* - These are inputs that are unobservable for the asset or liability.

The carrying value of the Company's cash, accounts receivable and accounts payable approximates their fair values based on the short-term nature of such items. The carrying value of the installment debt and secured line of credit approximates fair value since the interest rate is at terms currently available to the Company.

### *Inventories*

Inventories are stated at the lower of cost or net realizable value, with cost determined on the first-in, first-out basis.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### *Income Taxes*

The Company provides for income taxes and recognizes deferred tax assets and liabilities on the balance sheets using the liability method for income taxes. The liability method requires that all deferred tax balances be determined by using the applicable tax rate expected to be in effect when the taxes will actually be paid, or when refunds are received. The applicable tax rate is applied to the differences between the tax bases of assets and liabilities and to their reported amounts in the financial statements. The resulting deferred tax asset or liability is adjusted to reflect changes in tax laws as they occur. Valuation allowances are established, if necessary, to reduce the deferred tax assets and liabilities (see Note 10).

In November 2015 the FASB issued ASU 2015-17 as part of its Simplification Initiative. The amendments eliminate the guidance in ASC 740, "Income Taxes," that required an entity to separate deferred tax liabilities and assets between current and noncurrent amounts in a new classified balance sheet. Rather, deferred taxes are permitted to be presented as noncurrent under the new standard as a single line item. This pronouncement is required to take effect for fiscal years starting after December 15, 2017 for private companies.

### *Depreciation and Amortization*

Depreciation and amortization are provided principally on the straight-line method over the estimated useful lives of the related assets, as follows:

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Machinery and equipment	5 years
Office furniture and equipment	3-7 years
Computer equipment and software costs	3-5 years
Tools, dies and molds	3 years

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Leasehold improvements are amortized over the lesser of the estimated useful life of the asset or the term of the lease.

Expenditures for maintenance and repairs are expensed as incurred, while renewals and betterments that materially extend the life of an asset are capitalized. The cost of assets sold, retired, or otherwise disposed of, and the related allowance for depreciation, are eliminated from the accounts, and any resulting gain or loss is recognized.

### *Patents*

The Company owns various patents of technology concerning its electronic metering systems and processes. The costs associated with the acquisition of patents, and the costs of registering the patents, are capitalized and amortized on the straight-line basis over their remaining lives. Amortization expense for the fiscal years ended February 28, 2019 and 2018 amounted to approximately \$25,500 and \$25,000, respectively.

### *Trademarks*

The Company owns two trademarks in various countries. The cost of registering the trademarks are capitalized and amortized on the straight-line basis over the remaining lives. Amortization expense

# Quadlogic Controls Corporation

## Notes to Financial Statements

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for the fiscal years ended February 28, 2019 and 2018 amounted to approximately \$2,300 for each year.

### *Research and Development*

Research and development costs are expensed as incurred.

### *Shipping and Handling*

Shipping and handling costs incurred in shipping products to customers are expensed as incurred and included in cost of meters sold. Shipping costs totaled approximately \$104,000 and \$122,000 for the fiscal years ended February 28, 2019 and 2018, respectively. All shipping and handling costs billed to customers are recorded in revenue.

### *Stock-Based Compensation*

The Company follows the provisions of ASC 718 for stock-based compensation. This statement requires entities to measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award over the service period.

## 2. Concentration of Credit Risk

The Company maintains its cash balances in financial institutions in New York. From time to time, the Company has cash balances that may exceed federally insured limits.

The Company's trade receivables are potentially subject to credit risk. The Company extends credit to its customers based upon an evaluation of the customers' financial condition and credit history. The Company's policies do not require collateral to support accounts receivable. However, because of the diversity and creditworthiness of the individual accounts that comprise the total balance, management does not believe that the Company is subject to any significant credit risk.

For the fiscal years ended February 28, 2019 and 2018, revenues derived from two customers amounted to \$2,373,988 or 16.4% and \$2,328,843 or 16.9% of total revenues, respectively. As of February 28, 2019 and 2018, accounts receivable from three customers accounted for 32.1% and 32.6% of total receivables, respectively.

## 3. Inventories

Inventories, net consisted of the following:

<i>February 28,</i>		2019		2018
Raw materials	\$	238,002	\$	453,599
Work-in-progress		408,185		504,959
Finished goods		362,703		402,473
<b>Total Inventories, Net</b>	<b>\$</b>	<b>1,008,890</b>	<b>\$</b>	<b>1,361,031</b>

As of February 28, 2019 and 2018, the Company has inventory reserves of approximately \$509,000 and \$166,000, respectively, which has been allocated across each of the inventory categories.

# Quadlogic Controls Corporation

## Notes to Financial Statements

Approximately \$402,000 of the inventory reserves as of February 28, 2019 related to the Energy Guard product line and this amount had also been recorded to cost of goods sold in fiscal 2019.

### 4. Property and Equipment

Property and equipment consisted of the following:

<i>February 28,</i>	2019	2018
Machinery and equipment	\$ 1,221,744	\$ 1,229,919
Office furniture and equipment	414,204	416,141
Leasehold improvements	1,554,046	1,574,146
Computer equipment and software costs	313,792	181,177
Tools, dies and molds	184,005	242,860
	<b>3,687,791</b>	<b>3,644,243</b>
Less: accumulated depreciation and amortization	<b>(2,873,119)</b>	<b>(2,995,593)</b>
<b>Property and Equipment, Net</b>	<b>\$ 814,672</b>	<b>\$ 648,650</b>

Included in computer equipment and software costs are construction-in-process software assets with a cost of \$180,000, which had not yet been placed into service as of February 28, 2019. There were no construction-in-process assets as of February 28, 2018.

The Company disposed of \$320,000 worth of fully depreciated fixed assets in the fiscal year ended February 28, 2019, for no gain or loss, and disposed of \$65,000 worth of fixed assets, for a \$35,000 loss, in the fiscal year ended February 28, 2018.

Depreciation and amortization expense for the fiscal years ended February 28, 2019 and 2018 amounted to approximately \$197,000 and \$186,000, respectively.

### 5. Intangible Assets

The components and weighted average amortization period of intangible assets are as follows:

<i>February 28,</i>	2019	2018	Weighted Average Amortization Period
Patents	\$ 510,499	\$ 498,617	18 years
Trademarks	29,964	29,964	10 years
<b>Gross Intangibles</b>	<b>540,463</b>	<b>528,581</b>	
Less: accumulated amortization (patents)	<b>(154,074)</b>	<b>(128,559)</b>	
Less: accumulated amortization (trademarks)	<b>(16,754)</b>	<b>(14,406)</b>	
<b>Intangibles, net of amortization</b>	<b>\$ 369,635</b>	<b>\$ 385,616</b>	

The aggregate amortization expense related to intangible assets for the next five years is as follows:

# Quadlogic Controls Corporation

## Notes to Financial Statements

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*Year ending February 28,*

2020	\$	31,358
2021		31,358
2022		31,042
2023		29,009
2024		28,815
2025 and thereafter		218,053
<b>Total</b>	<b>\$</b>	<b>369,635</b>

### 6. Secured Credit Line

On October 1, 2012, the Company entered into a new loan agreement which permitted borrowings of up to \$2,000,000 under a revolving line of credit facility. The loan agreement shall automatically renew from year to year thereafter until amended or terminated by either party. On January 22, 2018, the loan agreement was amended until October 31, 2019 and on June 6, 2019, the loan agreement was amended further until October 31, 2021. The maximum loans and advances against accounts receivable is \$2,000,000 and against inventory is \$250,000. The lender agreed, at the borrower's request, to periodically re-evaluate the total facility, and may increase the facility, but not to exceed \$5,000,000. This line of credit is secured by the Company's trade receivables, deposit accounts, equipment, machinery, and furniture and fixtures. Borrowings under the credit facility bear interest at prime plus 3% for loans made against accounts receivable, and interest at prime plus 5% for loans made against inventory. The minimum monthly interest charge is \$4,000 for a credit line of \$1,250,000 and increases to \$5,000 when the total credit line exceeds \$1,250,000. The agreement includes collateral monitoring fees and an annual facility fee of 2% on the line of credit. The amount borrowed at February 28, 2019 and 2018 was approximately \$1,102,000 and \$938,000, respectively.

### 7. Capital Lease Obligations

On July 10, 2018, the Company entered into a five-year loan agreement with Crestmark Equipment Finance to finance \$133,793 of computer equipment. The loan represents an unsecured obligation and bears interest at a rate of 8.85% per year. The loan required a down payment of \$5,538 with the principal balance of \$128,255 plus interest to be paid ratably with monthly payments of \$2,769 over the remaining 48 months.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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Future minimum lease payments for the capital leases are as follows:

*Fiscal year ending February 28,*

2020	\$	33,228
2021		33,228
2022		33,228
2023		33,228
2024		13,845
<b>Total</b>		<b>146,757</b>
Less: amount representing interest		(25,718)
<b>Present Value of Net Minimum Lease Payments</b>		<b>121,039</b>
Less: current maturities of capital leases		(23,448)
<b>Capital Lease Obligation, net of current maturities</b>	<b>\$</b>	<b>97,591</b>

### 8. Convertible Preferred Stock

The Company is authorized to issue 5,000,000 shares of \$.001 par value preferred stock, including 4,000,000 shares of Series A convertible preferred stock. The shares may be designated and issued by the Board of Directors at any time in one or more series that will have voting rights, mandatory interest, convertible features, and/or preferences that have not been given to shares of any other series of the Company's common stock. No shares were issued or outstanding as of February 28, 2019 and 2018.

Series A convertible preferred stock accrues cumulative dividends at the rate of 9% per annum, which are payable if and when declared by the Company's Board. Each share of preferred stock is convertible into 1.25 shares of common stock at the option of the holder at any time.

### 9. Commitments

In fiscal year 2007, the Company entered into a lease agreement for new facilities. The lease commenced July 1, 2007 and expires June 30, 2022. The lease is for a 15-year period, with an option to buy out the remainder of the lease term at the end of 10 years. The lease provides for minimum annual rentals plus real estate taxes and escalation charges. The facilities are located within an area that qualifies the Company for certain New York City income tax credits.

Rent expense charged to operations, net of income tax credits, amounted to approximately \$1,004,870 and \$991,000 for the fiscal years ended February 28, 2019 and 2018, respectively.

# Quadlogic Controls Corporation

## Notes to Financial Statements

Future minimum annual rental payments under the non-cancelable operating lease are as follows:

*Fiscal year ending February 28,*

2020	\$	943,916
2021		943,916
2022		943,916
2023		314,639
	\$	3,146,387

### *Concentration of Vendors*

The Company relies on a limited number of outside vendors who currently supply necessary components for the manufacture of meters. The Company is subject to the risk that it may not be able to obtain sufficient quantities or reasonable prices. The Company purchased inventory and services from its three largest vendors of \$1,234,824 and \$1,180,195 for the years ended February 28, 2019 and 2018, respectively. This represents 25.8% and 23.2% of the total purchases for years ended February 28, 2019 and 2018, respectively.

## 10. Income Taxes

Deferred tax assets arise from net operating loss carryforwards and from items that are currently expensed for financial statement purposes but are not currently deductible for income tax purposes. The components of the deferred tax asset are as follows:

<i>February 28,</i>	2019	2018
<b>Deferred Tax Assets</b>		
Net operating loss carryforwards	\$ 757,777	\$ 516,794
R&D credit carryforwards	1,106,085	1,019,735
REAP credit carryforward	933,100	1,098,638
Wage reduction credit	19,200	9,600
Accrued expenses	177,925	214,145
Deferred rent	108,804	172,049
Other reserves	193,245	140,587
Tax capitalization of certain inventory costs	21,862	38,573
Royalty income	-	180,850
<b>Total Deferred Tax Assets</b>	<b>3,317,998</b>	<b>3,390,971</b>
<b>Deferred Tax Liability</b>		
Depreciation	(44,544)	(20,127)
<b>Total Deferred Tax Assets</b>	<b>3,273,454</b>	<b>3,370,844</b>
Less: valuation allowance	(3,273,454)	(3,370,844)
<b>Net Deferred Tax Asset</b>	<b>\$ -</b>	<b>\$ -</b>

The Company has established a full valuation allowance against its deferred tax assets due to the uncertainty surrounding realization of such assets.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the Act) was signed into law. Among other things, the Act reduced the Company's corporate federal tax rate to a flat 21%. As a result, the Company's deferred tax items are measured at an effective tax rate of 19.76% for federal tax purposes as of February 28, 2019.

As of February 28, 2019, the Company had federal, state and city net operating loss carryforwards of approximately \$2,951,446 available to reduce any future federal, state and city taxable income. The federal, state and city net operating loss carryforwards begin expiring in February 28, 2030.

The Company has Federal R&D credit carryforwards of \$1,106,085 that begin to expire February 28, 2020. The Company also has NYC REAP credits of \$933,100 that have been reduced by expiring credits of \$171,726 that expired as of February 28, 2019. As the REAP credits have only a 5-year carryforward period, credits have begun to expire and some amount of credit will be lost each year if not used.

The Company follows ASC 740-10 (FASB Interpretation No. 48) "Accounting for Uncertainty in Income Taxes," which clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statement disclosure of tax provisions taken or expected to be taken on a tax return. The Company has not identified any uncertain tax positions that would require a provision of a liability under ASC 740-10.

Open tax years for federal income taxes are fiscal years ended 2019, 2018, 2017, and 2016. Open tax years for state income taxes range between three to four years or for fiscal years ended 2016 to 2019.

The Company's policy is to recognize interest and penalties relating to uncertain tax positions in income tax expense.

### 11. Employee Stock Awards and Warrants

#### *Common Stock*

During fiscal 2019 the Company compensated each independent director \$40,000 and granted 215,000 shares of the Company's common stock to its directors, which vested immediately and for the year ended February 28, 2019. The grant date fair value for the 95,000 and 120,000 shares, which had been granted on June 25, 2018 and October 4, 2018, were \$0.25 and \$0.37 per share, respectively. Stock compensation costs relating to the director shares was \$68,150. During fiscal 2018, the Company compensated each independent director \$40,000.

#### *Restricted Stock*

The Company granted 200,000 restricted shares to various employees on January 31, 2019. Vesting terms are time-based and stipulate that 25% of the restricted shares will be vested on the grant date, while an additional 25% of the shares will vest on the first, second and third anniversary dates of the grants until the restricted shares are fully vested. No restricted shares had been granted to the Company's employees during 2018. The Company recognized \$15,000 in compensation expense from the 50,000 restricted share awards issued to employees that vested in the fiscal year ended February 28, 2019.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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On April 1, 2019, the Company granted 135,000 shares of restricted stock to an employee of the Company.

The following table reflects the activity of restricted shares:

	Shares	Weighted Average Grant Date, Fair Value
Unvested, February 28, 2018	-	\$ -
Granted	200,000	0.30
Vested	(50,000)	0.30
Forfeited	-	-
Unvested, February 28, 2019	150,000	\$ 0.30

As of February 28, 2019, the total unrecognized compensation cost for the unvested restricted shares was \$45,000 and is to be recognized over a weighted average period of approximately 2.9 years.

### *Options*

As of February 28, 2019 and 2018, there were no outstanding employee or director options.

### *Warrants*

The Company has granted warrants to purchase shares of its common stock in connection with various equity transactions. There were 249,760 warrants outstanding during the years ended February 28, 2019 and 2018.

There were no warrants issued for fiscal years ended February 28, 2019 and 2018.

The Company uses the Black-Scholes pricing model to value warrants. The value of each warrant granted is estimated on the date of the grant.

## 12. Related-Party Transactions

Installment debt represents accumulated interest that accrued on unpaid compensation payable to one of the Company's officers (who is also a significant shareholder). The obligation is unsecured and bears interest at 6% per annum. Accrued Interest paid during the fiscal years ended February 28, 2019 and 2018 was \$26,497 and \$33,350, respectively. The current portion at February 28, 2019 and 2018 is \$376,852 and \$118,467, respectively, and the monthly payment is \$12,080. For the year ended February 28, 2019, the full balance is current, as the debt can be called at any time by the officer. For the year ended February 28, 2018, \$376,852 was classified as non-current, as the officer had agreed to not call the unpaid balance during the fiscal 2019 year.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 13. Litigation

From time to time, the Company is involved in routine litigation that arises in the ordinary course of business. There are no pending significant legal proceedings to which the Company is a party for which management believes the ultimate outcome would have a material adverse effect on the Company's financial position. On January 16, 2018, the Company filed a lawsuit against its Mexican licensee, alleging, among other things, breach of contract, failure to pay royalties, and payment of royalties in the amount of \$7,360,000. On January 2, 2019, the Company was awarded a default judgement by the United States District Court, Southern District of New York in the amount of \$7,360,000 plus pre-judgement interest in the amount \$615,773 against Pounce Electronics S.A. DE C.V., the Mexican licensee. There are no assurances of recovery, but the Company is pursuing all legal channels.

### 14. Subsequent Events

Subsequent events have been evaluated through June 27, 2019, which is the date the financial statements were available to be issued.