



LOYYAL CORPORATION AND SUBSIDIARIES
Consolidated Financial Statements
December 31, 2018 and 2017
With Independent Auditors' Report

Loyyal Corporation and Subsidiaries
December 31, 2018 and 2017

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INDEPENDENT AUDITORS' REPORT

To the Stockholders and Board of Directors,
Loyyal Corporation and Subsidiaries:

We have audited the accompanying consolidated financial statements of Loyyal Corporation and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations, comprehensive loss, changes in stockholders' equity (deficit) and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these 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 control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 audits 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 the auditors' 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, the auditor considers internal control relevant to the entity'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 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 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 Loyyal Corporation and Subsidiaries as of December 31, 2018 and 2017, 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.

Withum Smith & Brown, PC

August 6, 2019

Loyyal Corporation and Subsidiaries
Consolidated Balance Sheets
December 31, 2018 and 2017

	2018	2017
Assets		
Current assets		
Cash	\$ 177,603	\$ 725,879
Short-term investments, at fair value	2,412	10,537
Accounts receivable - net	92,750	108,689
Prepaid expenses and other current assets	54,403	32,903
Loans due from stockholder	100,000	3,100
Total current assets	<u>427,168</u>	<u>881,108</u>
Property and equipment - net	16,257	12,494
Goodwill and other intangible assets	12,955	54,634
Other assets	<u>15,093</u>	<u>21,904</u>
	<u>\$ 471,473</u>	<u>\$ 970,140</u>
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities		
Current portion of convertible promissory notes payable	\$ 100,000	\$ --
Loans payable - related parties	11,662	36,662
Accounts payable	94,708	49,186
Accrued expenses and other current liabilities	115,510	59,647
Total current liabilities	<u>321,880</u>	<u>145,495</u>
Convertible promissory notes payable, net of current portion	800,000	--
Stockholders' equity (deficit)		
Preferred stock, 0.001 par value, (liquidation value of \$6,631,902 and \$5,131,902 in 2018 and 2017, respectively); 24,672,351 and 20,522,132 shares authorized; 24,672,351 and 20,001,637 shares issued and outstanding at December 31, 2018 and 2017, respectively	24,673	20,002
Common stock, 0.001 par value; 52,500,000 and 45,500,000 shares authorized; 15,216,624 and 15,097,844 shares issued and 11,861,233 and 15,097,844 shares outstanding at December 31, 2018 and 2017, respectively	2,564	2,445
Additional paid-in capital	7,462,002	5,864,024
Less: Treasury stock; 3,355,391 shares at cost	(526,524)	--
Accumulated deficit	(7,613,122)	(5,057,319)
Accumulated other comprehensive loss	--	(4,507)
Total stockholders' equity (deficit)	<u>(650,407)</u>	<u>824,645</u>
	<u>\$ 471,473</u>	<u>\$ 970,140</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

Loyyal Corporation and Subsidiaries
Consolidated Statements of Operations
Years Ended December 31, 2018 and 2017

	2018	2017
Revenues	\$ 396,631	\$ 293,689
Operating expenses		
Sales and marketing	1,629	18,516
General and administrative	2,803,677	2,275,108
Stock based compensation expense	80,663	111,184
Depreciation and amortization	10,035	7,507
	<u>2,896,004</u>	<u>2,412,315</u>
Loss from operations	(2,499,373)	(2,118,626)
Other income (expense)		
Interest expense	(19,453)	(531,707)
Realized and unrealized (loss) gain on short-term investments	(8,125)	9,461
Loss on debt forgiveness	(9,041)	--
Total other expense	<u>(36,619)</u>	<u>(522,246)</u>
Loss from continuing operations	(2,535,992)	(2,640,872)
Loss from discontinued operations	<u>(19,811)</u>	<u>--</u>
Net loss	<u>\$ (2,555,803)</u>	<u>\$ (2,640,872)</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

Loyyal Corporation and Subsidiaries
Consolidated Statements of Comprehensive Loss
Years Ended December 31, 2018 and 2017

	2018	2017
Net loss	\$ (2,555,803)	\$ (2,640,872)
Other comprehensive loss		
Change in foreign currency translation adjustment	<u>4,507</u>	<u>(4,507)</u>
Comprehensive loss	<u>\$ (2,551,296)</u>	<u>\$ (2,645,379)</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

Loyyal Corporation and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity (Deficit)
Years Ended December 31, 2018 and 2017

	Series Seed Preferred Stock		Series A Preferred Stock		Series A-1 Preferred Stock		Series A-2 Preferred Stock		Series A-3 Preferred Stock		Common Stock		Treasury Stock		Additional	Accumulated	Accumulated	Total
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Paid-in Capital	Deficit	Other Comprehensive Loss	Stockholders' Equity (Deficit)
Balance, January 1, 2017	5,528,705	\$ 5,529	--	\$ --	--	\$ --	--	\$ --	--	\$ --	14,125,288	\$ 1,472	--	\$ --	\$ 1,833,575	\$ (2,416,447)	\$ --	\$ (575,871)
Issuance of Series A Preferred Stock	--	--	7,286,783	7,287	--	--	--	--	--	--	--	--	--	--	1,952,712	--	--	1,959,999
Issuance of Series A-1 and A-2 Preferred Stock upon conversion of Convertible Debt	--	--	--	--	6,771,499	6,771	414,650	415	--	--	--	--	--	--	1,448,123	--	--	1,455,309
Beneficial conversion feature related to convertible debt	--	--	--	--	--	--	--	--	--	--	--	--	--	--	477,624	--	--	477,624
Issuance of Common Stock	--	--	--	--	--	--	--	--	--	--	972,556	973	--	--	40,806	--	--	41,779
Stock-based compensation	--	--	--	--	--	--	--	--	--	--	--	--	--	--	111,184	--	--	111,184
Net loss	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	(2,640,872)	--	(2,640,872)
Foreign currency translation adjustment	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	(4,507)	(4,507)
Balance, December 31, 2017	<u>5,528,705</u>	<u>\$ 5,529</u>	<u>7,286,783</u>	<u>\$ 7,287</u>	<u>6,771,499</u>	<u>\$ 6,771</u>	<u>414,650</u>	<u>\$ 415</u>	<u>4,670,714</u>	<u>\$ 4,671</u>	<u>15,097,844</u>	<u>\$ 2,445</u>	<u>--</u>	<u>--</u>	<u>5,864,024</u>	<u>(5,057,319)</u>	<u>(4,507)</u>	<u>824,645</u>
Issuance of Series A-3 Preferred Stock	--	--	--	--	--	--	--	--	4,670,714	4,671	--	--	--	--	1,495,329	--	--	1,500,000
Purchase of Common Stock into treasury	--	--	--	--	--	--	--	--	--	--	(3,355,391)	--	3,355,391	(526,524)	--	--	--	(526,524)
Exercise of stock options	--	--	--	--	--	--	--	--	--	--	275,792	276	--	--	21,829	--	--	22,105
Cancellation of common stock	--	--	--	--	--	--	--	--	--	--	(157,012)	(157)	--	--	157	--	--	--
Stock-based compensation	--	--	--	--	--	--	--	--	--	--	--	--	--	--	80,663	--	--	80,663
Net loss	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	(2,555,803)	--	(2,555,803)
Foreign currency translation adjustment	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	4,507	4,507
Balance, December 31, 2018	<u>5,528,705</u>	<u>\$ 5,529</u>	<u>7,286,783</u>	<u>\$ 7,287</u>	<u>6,771,499</u>	<u>\$ 6,771</u>	<u>414,650</u>	<u>\$ 415</u>	<u>4,670,714</u>	<u>\$ 4,671</u>	<u>11,861,233</u>	<u>\$ 2,564</u>	<u>3,355,391</u>	<u>\$ (526,524)</u>	<u>\$ 7,462,002</u>	<u>\$ (7,613,122)</u>	<u>\$ --</u>	<u>\$ (650,407)</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

Loyyal Corporation and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended December 31, 2018 and 2017

	2018	2017
Cash flows from operating activities		
Net loss	\$ (2,555,803)	\$ (2,640,872)
Adjustments to reconcile net loss to net cash used by operating activities		
Depreciation and amortization	10,035	7,507
Bad debt expense	150,000	--
Net realized and unrealized loss (gain) on short-term investments	8,125	(9,461)
Loss on discontinued operations	42,740	--
Loss on debt forgiveness	9,041	--
Stock based compensation expense	80,663	111,184
Beneficial conversion feature interest expense	--	477,624
Changes in operating assets and liabilities		
Accounts receivable	(134,061)	49,338
Prepaid expenses and other current assets	(21,500)	74,825
Other assets	(2,230)	(18,209)
Accounts payable	45,522	28,687
Accrued expenses and other current liabilities	54,802	27,574
Net cash used by operating activities	<u>(2,312,666)</u>	<u>(1,891,803)</u>
Cash flows from investing activities		
Proceeds from sales of short-term investments	--	4,736
Capital expenditures	<u>(13,798)</u>	<u>(8,044)</u>
Net cash used by investing activities	<u>(13,798)</u>	<u>(3,308)</u>
Cash flows from financing activities		
Proceeds from the sale of convertible promissory notes	900,000	105,000
Issuance of loans receivable - stockholder	(100,000)	--
Principal repayment of loan receivable - stockholder	3,100	--
Decrease in loans due to stockholders	--	(76,227)
Principal repayment of loans payable - related parties	(25,000)	(10,000)
Cash contributions for preferred stock	1,500,000	1,959,999
Purchase of stock into treasury	(526,524)	--
Proceeds from the exercise of stock options	22,105	--
Net cash provided by financing activities	<u>1,773,681</u>	<u>1,978,772</u>
Net change in cash	(552,783)	83,661
Effect of exchange rates on cash	4,507	(4,581)
Cash		
Beginning of year	<u>725,879</u>	<u>646,799</u>
End of year	<u><u>\$ 177,603</u></u>	<u><u>\$ 725,879</u></u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

Loyyal Corporation and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2018 and 2017

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of Operations

Loyyal Corporation and Subsidiaries, (the "Company") is a computer software company that has developed a universal loyalty and rewards platform, with blockchain and smart contract technology. The platform offers interoperability to the loyalty program industry including multi-branded coalitions, superior program liability management and dynamic issuance/redemption options customized for each unique relationship.

Loyyal Corporation was formed as a corporation in the State of Delaware on August 12, 2014, under the original name of Ribbit.me! USA Inc. In February 2017, the name was changed to Loyyal Corporation.

In 2017, Loyyal Corporation purchased Qobolo Limited ("Qobolo"), a limited-liability company located in the United Kingdom, and changed their name to Loyyal UK Ltd. In January 2018 Qobolo ceased operations and in December 2018, the Company dissolved Qobolo and recognized a loss from discontinuing operations of approximately \$19,811 (see also Note 8).

In March 2017, the Company formed a subsidiary, Loyyal MENA FZ-LLC ("Dubai"), a Dubai limited-liability company. As of December 2018 this subsidiary has not commenced operations.

Principles of Consolidation

The consolidated financial statements include the accounts of Loyyal Corporation and its wholly owned subsidiaries, Qobolo and Dubai. All significant intercompany balances and transactions have been eliminated in consolidation.

Stockholder's Deficit and Management's Plan

The Company has a total stockholder's deficit of \$650,407 at December 31, 2018 and a net loss of \$2,555,803 for the year ended December 31, 2018. Since its formation, the Company's management has been dependent on both debt and equity financing as it works towards its goals of revenue growth and profitability. The Company's management anticipates incurring additional future losses while working to secure new contracts and managing controllable expenses. Management plans to continuously secure additional investment to sustain its operations. Subsequent to year end, the Company executed a stock purchase agreement providing for the issuance and sale of up to \$3,000,000 of Series B Preferred Stock (see Note 12).

The Company's ability to fund deficits is dependent on the success of management's plans. The accompanying consolidated financial statements do not include any adjustments that might be necessary related to recoverability or classification of recorded assets or the amounts or classification of liabilities in the event that management's plans are not successful.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of consolidated 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 disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amount of revenues and expenses during the reporting period. The most significant estimates relate to the accounting for equity share based compensation. Actual results could differ from these estimates.

Reclassifications

Certain amounts presented in the prior year have been reclassified to conform to current year consolidated financial statement presentation. These reclassifications have no effect on previously reported net income.

Loyyal Corporation and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2018 and 2017

Cash and Concentrations of Credit Risk

Cash includes amounts on deposit in banks. Cash accounts at each institution are insured by the Federal Deposit Insurance Corporation. At times, cash balances in the Company's accounts may exceed federally insured limits. All bank accounts exceeding FDIC insurable limits are with major financial institutions.

Short-Term Investments

Short-term investments consist of crypto-currency investments that are generally used in operations. Such investments are classified as trading securities and are recorded at fair market value with the change in fair value during the year included in the Company's consolidated statements of operations.

Accounts Receivable, Credit Policy and Customer Concentrations

Accounts receivable are uncollateralized customer obligations due under normal trade terms requiring payment within 30 days from the invoice date.

Accounts receivable are stated at the amount billed to the customer and do not bear interest. The Company reviews its accounts receivable on a monthly basis to determine the necessity of an allowance.

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of the amounts that will not be collected. The Company considers a number of factors, including the length of time accounts receivable are past due, the Company's previous loss history, if applicable, the customer's current ability to pay its obligation and the condition of the economy. At December 31, 2018 and 2017, there was no allowance for doubtful accounts.

Credit risk with respect to customers is concentrated as follows:

- During 2018, the Company derived revenue from sales to six different customers, each comprising at least 10% of total revenue (ranging from 10% - 38%). As of December 31, 2018, two of these customers accounted for approximately 94% of outstanding accounts receivable (51% and 43%).
- During 2017, the Company derived revenue from sales to two customers comprising approximately 89% of total revenue (48% and 41%). As of December 31, 2017, three customers accounted for all outstanding accounts receivable (46%, 42% and 12%).

Property and Equipment

Property and equipment are stated at cost and are depreciated on a straight-line basis over the estimated useful lives of the underlying assets. Repairs and maintenance are charged to expense as incurred. Expenditures for major renewals and betterments that extend the useful lives of the assets are capitalized.

Impairment of Long-Lived Assets

The Company is required to review long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. When an evaluation is required, the estimated future undiscounted cash flows associated with the assets are compared to the assets' carrying amount to determine if a write-down to fair value is necessary. Management believes that there have been no impairments of the Company's long-lived assets as of December 31, 2018 and 2017.

Goodwill and Other Intangible Assets

The Company evaluates the recoverability of goodwill on an annual or more frequent basis as events or changes in circumstances indicate that the carrying value of the asset may be impaired. An impairment loss is recognized when the fair value or the estimated future cash flows expected to result from the use of the asset, including disposition, is less than the carrying value of the asset. Professional standards provide that intangible assets with finite useful lives be amortized and intangible assets with indefinite lives not be amortized, but be tested at least annually for impairment. In addition, the Company tests its goodwill on an annual basis for impairment. The Company identified all reporting units which constitute components of the Company's goodwill and, during 2018 and 2017, the Company completed its annual impairment test on a qualitative basis and determined that goodwill was not impaired. During 2018, however, the Company wrote-down \$41,679 of goodwill associated with Qobolo as part of its accounting for discontinued operations.

Revenue Recognition

The Company derives revenue from licensing the use of their data products pursuant to contractual obligations. The Company begins recognizing the related revenue when the license is delivered and accepted by the customer with the total amount being spread evenly over the term of the agreement.

Research and Development

New product research and development costs are charged to operations as incurred and are included primarily in general and administrative. Research and developments costs consist primarily of payroll and related costs and fees paid to consultants and outside service providers.

Advertising Costs

Advertising costs are charged to operations in the years incurred and approximated \$1,629 and \$18,516 for the years ended December 31, 2018 and 2017, respectively.

Stock Based Compensation

The Company accounts for stock-based compensation in accordance with professional standards, which require that equity awards issued to employees and non-employees be valued at their fair value.

The fair value of stock options is determined using the Black-Scholes valuation model. Such value is recognized as expense on a straight-line basis over the service period, net of estimated forfeitures. The estimation of stock awards that will ultimately vest requires judgment and, to the extent that actual results or updated estimates differ from the Company's current estimates, such amounts will be recorded as a cumulative adjustment in the period estimates are revised. Actual results and future changes in estimates may differ from the Company's current estimates.

Income Taxes

Income taxes have been provided in accordance with ASC Topic 740 – *Income Taxes*. ASC Topic 740 requires that deferred tax assets and liabilities be recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period when the change in tax rates is enacted. A valuation allowance is established when it is determined that it is more likely than not that some portion of all deferred tax assets will not be realized.

Loyyal Corporation and Subsidiaries
Notes to Consolidated Financial Statements
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The Company follows *Accounting for Uncertainty in Income Taxes*, which is now included as part of ASC Topic 740 – *Income Taxes*. This section of the ASC clarifies the accounting for uncertainty in income taxes recognized in an entity's consolidated financial statements and prescribes a recognition threshold of more-likely-than-not to be sustained upon examination. Measurement of the tax uncertainty occurs if the recognition threshold has been met. The standard also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition requirements.

The Company files tax returns in the U.S. federal jurisdiction as well as certain state jurisdictions and has no income tax related penalties or interest for the periods presented in these consolidated financial statements. In the normal course of business, the Company is subject to examination by taxing authorities. As of December 31, 2018 and through the date of this report there are no ongoing audits or unresolved disputes with the various tax authorities that the Company files with. As of December 31, 2018 and 2017, the Company had no unrecognized tax benefits.

The Company's subsidiaries are subject to their respective country's tax law (Anguilla, United Kingdom and Dubai).

Foreign Currency Translation

The Company has foreign operations where the functional currency has been determined to be the local currency. The functional currency of the Company's subsidiary in Anguilla has been determined to be the Eastern Caribbean Dollar. The functional currency for the Company's subsidiary in the United Kingdom has been determined to be the British Pound Sterling. The functional currency of the Company's subsidiary in Dubai has been determined to be the United Arab Emirates Dirham. For transactions where the local currency is the functional currency, assets and liabilities are translated using end-of-period exchange rates; revenues, expenses and cash flows are translated using average rates of exchange. For these operations, currency translation adjustments are accumulated in a separate component of stockholders' equity (deficit). Transaction gains and losses are recognized in the determination of net income or loss. Aggregate foreign currency transaction gains and losses were not significant to these consolidated financial statements in 2018 or 2017.

Comprehensive Income (Loss)

The established standards for reporting comprehensive income (loss) include reporting and displaying comprehensive income (loss) and its components (revenues, expenses, gains and losses) in a full set of general-purpose financial statements. The Company's other comprehensive income (loss) component results from foreign currency translation adjustments.

Recent Accounting Pronouncements

In May 2014 the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), which supersedes all existing revenue recognition requirements, including most industry-specific guidance. Together with subsequent amendments, this created Accounting Standards Codification Topic 606 ("ASC 606"). ASC 606 requires an entity to recognize revenue when it transfers goods or services to customers in an amount that reflects the consideration that the entity expects to receive for those goods or services. ASC 606 also expands disclosure requirements. ASC 606 will be effective for the Company beginning January 1, 2019. ASC 606 allows for either "full retrospective" adoption, meaning the standard is applied only to the most current period presented in the financial statements. The Company is currently evaluating the impact of adoption of ASC 606 and, at this time, management believes that ASC 606 will have minimal impact on its consolidated financial statements.

Loyyal Corporation and Subsidiaries
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In February 2016 the FASB issued ASU 2016-02, *Leases* (Topic 842), which requires lessees to recognize most leases on the balance sheet. The ASU will be effective for the Company beginning January 1, 2020, unless deferred, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this ASU on its consolidated financial statements.

3. INVESTMENTS

The Company's investments in securities are comprised of digital currency.

Accounting principles generally accepted in the United States of America define fair value as the price that would be received to sell an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date. The Company's fair market valuations are based on quoted prices in active markets for identical securities that management has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in the active market, valuation of these securities does not entail a significant degree of judgment. As such, all investments at December 31, 2018 and 2017 were valued using Level 1 inputs.

Net realized and unrealized (losses) gains on securities was \$(8,125) and \$9,461 for the years ended December 31, 2018 and 2017, respectively.

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following as of December 31:

	Estimated Useful Life (Yrs)	2018	2017
Computers and equipment	3	\$ 34,224	\$ 23,213
Furniture and fixtures	7	<u>1,062</u>	<u>1,062</u>
		35,286	24,275
Less: Accumulated depreciation		<u>19,029</u>	<u>11,781</u>
Property and equipment, net		<u>\$ 16,257</u>	<u>\$ 12,494</u>

Depreciation expense was \$10,035 and \$7,507 during 2018 and 2017, respectively.

5. CONVERTIBLE PROMISSORY NOTES PAYABLE

2016 and 2017 Convertible Notes Payable

As of January 1, 2017, the Company had a series of unsecured convertible promissory notes payable in the principal amount of \$1,292,249 and bearing interest at rates ranging up to 10%. As of January 1, 2017, the Company had accrued interest on these notes in the amount of \$14,857. The notes were due and payable upon the earlier to occur of a demand by one or more holders owning together in excess of 50% of the aggregate principal amount under the then outstanding notes ("majority-in-interest") at any time following May 31, 2017 ("maturity date") or upon demand by a majority-in-interest at any time following an event of default, as defined in the agreement. The maturity date could be extended one time without amendment of the original note by written election of a majority-in-interest, provided, however, that in no event shall the extended maturity date exceed six months from May 31, 2017.

Loyyal Corporation and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2018 and 2017

The notes were subject to automatically convert upon equity financing. Further, if prior to the maturity date and prior to a change of control, as defined in the agreements, the Company sold or issued equity securities (other than common stock) primarily for the purpose of raising capital in one or more transactions resulting in cumulative gross proceeds to the Company equal to at least \$10,000,000 (or in some cases \$6,500,000), not including for such purpose the outstanding principal amount of the notes and accrued interest, then upon the date of the closing of such equity financing, the then outstanding principal amount of the notes and all accrued interest would be automatically converted into such number of shares of the type of equity securities to be issued in the equity financing equal to the quotient obtained by dividing (a) the aggregate outstanding principal and unpaid accrued interest due on the notes on the day of conversion by (b) the applicable capped conversion price, as defined in the agreements, rounded down to the nearest whole number of shares.

If prior to the maturity date and prior to a change of control, the Company sold or issued equity securities (other than common stock) of less than \$10,000,000 (or in some cases \$6,500,000), not including for such purpose of the outstanding principal amount of the notes and accrued interest, the Company would provide each note holder with a written notice, and within ten days of receipt of such notice, a majority-in-interest would by written notice and on behalf of all of the note holders, elect to convert the then outstanding principal amount of the notes and all accrued interest into such number of shares of the type of equity securities to be issued in the equity financing equal to the quotient obtained by dividing (a) the aggregate outstanding principal and unpaid accrued interest due on the notes on the day of conversion by (b) the applicable conversion price, rounded down to the nearest whole number of shares.

If the notes were not converted pursuant to either of the above prior to the maturity date, a majority-in-interest may elect to convert the then outstanding principal amount of the notes and all accrued interest into such number of shares of the Company's Preferred stock equal to the quotient obtained by dividing (a) the aggregate outstanding principal and unpaid accrued interest due on the notes on the day of conversion by (b) capped conversion price, as defined in the agreements, rounded down to the nearest whole number of shares, by delivering a written notice to the Company specifying the date on which such conversion is to occur.

If a change of control, as defined in the agreements, occurred prior to the maturity date and prior to any conversion of the notes, then upon a change of control, the Company would pay to the note holders, in addition to the outstanding principal and accrued interest a "success payment" equal to 200% of the then outstanding principal.

In January 2017, two additional unsecured convertible promissory notes payable in the amount of \$105,000 were issued. The notes bore interest at 5% and were subject to same conversion features as described above. In addition, in May 2017, the Company amended its convertible promissory note agreements to lower the required proceeds in connection with the automatic conversion upon an equity financing from \$10,000,000 to \$1,500,000.

During 2017, all of the convertible promissory notes in the amount of \$1,455,309, which included accrued interest of \$58,060 converted into 6,771,499 shares of Series A-1 Preferred stock and 414,650 shares of Series A-2 Preferred Stock. The terms of the convertible promissory notes gave rise to a beneficial conversion feature totaling \$477,624 which has been recorded as interest expense in the consolidated statements of operations and comprehensive loss. The beneficial conversion feature was valued as the difference between the estimated fair value of the common stock issued and the carrying value of the convertible promissory notes and accrued interest that was converted.

2018 Convertible Notes Payable

On January 24, 2018, the Company issued two unsecured convertible promissory notes payable in the principal amount of \$900,000 and bearing at rates ranging up to 2.5% and maturing January 24, 2020. The notes were due and payable upon the earlier to occur of a demand by one or more holders owning together in excess of 50% of the aggregate principal amount under the then outstanding notes ("majority-in-interest") or upon demand by a majority-in-interest at any time following an event of default, as defined in the agreement. The maturity date may be extended one time without amendment of the original note by written election of the holder.

The notes were subject to automatically convert upon equity financing. Further, if prior to the maturity date and prior to a change of control, as defined in the agreements, the Company sold or issued equity securities (other than common stock) primarily for the purpose of raising capital in one or more transactions resulting in cumulative gross proceeds to the Company equal to at least \$16,500,000, then upon the date of the closing of such equity financing, the then outstanding principal amount of the notes and all accrued interest would be automatically converted into such number of shares of the type of equity securities to be issued in the equity financing equal to the quotient obtained by dividing (a) the aggregate outstanding principal and unpaid accrued interest due on the notes on the day of conversion by (b) the applicable capped conversion price, as defined in the agreements, rounded down to the nearest whole number of shares.

If the notes were not converted pursuant to either of the above prior to the maturity date, a majority-in-interest may elect to convert the then outstanding principal amount of the notes and all accrued interest into such number of shares of the Company's Preferred stock equal to the quotient obtained by dividing (a) the aggregate outstanding principal and unpaid accrued interest due on the notes on the day of conversion by (b) capped conversion price, as defined in the agreements, rounded down to the nearest whole number of shares, by delivering a written notice to the Company specifying the date on which such conversion is to occur.

6. STOCKHOLDERS' EQUITY

In January, 2018 the Company's Board of Directors amended its certificate of incorporation and authorized the Company to issue common and five series of preferred stock. The Company is authorized to issue up to 52,000,000 shares of Common Stock (par value \$0.001 per share) and 24,672,351 shares of Preferred Stock (par value \$0.001 per share), of which 5,528,705 have been designated as Series Seed Preferred Stock, 7,286,783 of which have been designated as Series A Preferred Stock, 6,771,499 of which have been designated as Series A-1 Preferred Stock, 414,650 of which have been designated as Series A-2 Preferred Stock and 4,670,714 of which have been designated as Series A-3 Preferred Stock. As of December 31, 2018, there were 6,712,596, of common stock reserved for future issuance.

The rights and privileges of the preferred and common stock are as follows:

Dividend Rights

The Company shall not pay or declare any dividends on shares of any other class or series of capital stock of the Company (other than dividends on shares of Common stock) unless the holders of each series of Preferred stock then outstanding shall get paid as defined in the operating agreements. No dividends were declared or paid as of December 31, 2018 and 2017.

Voting Rights

The holders of preferred stock and common stock shall vote together and not as separate classes. Each holder of outstanding shares shall be entitled to cast the number of votes equal to the number of whole shares of stock held by such holder.

Liquidation Preference

Upon liquidation of the Company, the holders of Preferred stock shall be entitled to receive, prior and in preference to any distribution of any assets of the Company to the holders of Common stock, an amount per share of Preferred stock held by them equal to the greater of the applicable original issue price (\$0.31049 per share for Series Seed, \$0.26898 per share for Series A, \$0.20184 per share for Series A-1, \$0.21518 per share for Series A-2, \$.32115 for Series A-3) plus any dividends declared but unpaid or such amount per share as would have been payable had all the shares of Preferred stock been converted into Common stock in accordance with the terms of the agreement. If upon liquidation the assets of the Company legally available for distribution to the holders of Preferred stock are insufficient to permit the payment to such holders of the full amount that they are entitled to, then the entire assets of the Company legally available for distribution shall be distributed in proportion to their respective amounts which would otherwise be payable in respect of the shares of Preferred stock held by them upon such distribution if such aggregate applicable liquidation preference were paid in full.

After payment to the holders of Preferred stock, the entire remaining assets of the Company shall be distributed pro rata to the holders of Common stock in proportion to the number of shares of Common stock held by the holders.

Conversion

The holders of Preferred stock shall have the right to convert each share of Preferred stock into Common stock determined by dividing the applicable original issue price (\$0.31049 per share for Series Seed, \$0.26898 per share for Series A, \$0.20184 per share for Series A-1 and \$0.21518 per share for Series A-2, \$.32115 for Series A-3) by the conversion price, as defined in the agreement. The conversion price applicable to a series of Preferred stock shall initially be equal to the applicable original issue price per share for such series of Preferred stock. No fractional shares of Common stock shall be issued upon conversion of Preferred stock. In lieu of any fractional shares, the Company shall pay cash equal to such fraction multiplied by the then fair market value of a share of Common stock as determined by the Board. In addition, the conversion is subject to adjustments for subdivisions of Common stock or Preferred stock as stipulated in the agreement.

7. STOCK-BASED COMPENSATION

Equity Incentive Plan

In 2015, the Company established an Equity Incentive Plan (the "Plan"), which reserved shares of Common stock for issuance in connection with various awards including incentive and nonqualified stock options and restricted stock to employees, members of the board, consultants or any other person that provides services to the Company. The Plan is administered by the board. Stock options are granted at fair value as determined by the board. Options granted under the Plan are generally vested over a four year period and are exercisable over a period not to exceed ten years. In 2017, the Company also revised its Equity Incentive Plan to authorize an additional 6,029,612 shares of common stock.

Further, in 2017, the Company issued common stock to some of the Company's investors as compensation for their services. In 2017 there was \$36,025 of compensation expense recognized, which represented the fair market value of the services performed.

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Stock-Based Compensation

The effect of recording stock-based compensation in 2018 and 2017 was as follows:

	2018	2017
Incentive stock options	\$ 71,542	\$ 71,679
Non-qualified stock options	2,984	3,480
Employee RSUs	6,137	--
Compensatory stock options to investors	--	36,025
	<u>\$ 80,663</u>	<u>\$ 111,184</u>

Valuation Assumptions

The determination of the fair value of the stock-based award is affected by highly subjective assumptions, including the deemed fair value of the underlying stock price on the grant date, the risk-free interest rate, the estimated volatility of the Company's stock price over the term of the award, the estimated period of time that the Company expects employees to hold their stock options and the expected dividend rate. These assumptions are as follows:

- Fair value of common stock: estimated by the Board of Directors based upon several factors, including recent transactions involving Company stock.
- Risk-free interest rate: based on the implied yield available on U.S. Treasury zero-coupon issues with an equivalent remaining term of the options.
- Volatility: based upon the price behavior of a group of guideline public companies, typically over several years, in order to calculate volatility to serve as a proxy for the Company's volatility.
- Expected term: estimated by taking the average of the vesting term and the contractual term of the option.
- Dividend yield: the Company has not paid and does not expect to pay any dividends.

Assumptions relating to stock option grants were as follows for 2018 and 2017:

	2018	2017
Fair value of common stock	\$0.09	\$0.08 – 0.09
Expected term (years)	10	10
Expected dividend yield	0%	0%
Risk-free interest rate	2.84 – 3.11%	2.21 – 2.84%

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Stock Options

The following table summarizes the Company's stock option unit activity for 2018 and 2017:

	Number of Shares	Weighted Average Exercise Price	Total Intrinsic Value	Weighted Average Remaining Contractual Life (Yrs)	Weighted Average Grant Date Fair Value
Outstanding – January 1, 2017	2,018,416	\$ 0.06	\$ --	9.58	\$ 0.04
Granted during 2017	5,596,004	0.08			
Exercised during 2017	--	--			
Cancelled during 2017	(1,345,634)	0.08			
Outstanding – December 31, 2017	6,268,786	0.08	--	9.19	0.05
Granted during 2018	2,480,860	0.09			
Exercised during 2018	(275,792)	0.08			
Cancelled during 2018	(2,171,846)	0.09			
Outstanding – December 31, 2018	<u>6,302,008</u>	<u>0.09</u>	<u>\$ --</u>	<u>8.87</u>	<u>\$ 0.06</u>
Vested and exercisable as of December 31, 2018	<u>3,047,562</u>	<u>\$ 0.06</u>		<u>7.55</u>	<u>\$ 0.08</u>

As of December 31, 2018 and 2017, there was \$248,173 and \$166,353, respectively, of total unrecognized compensation cost related to unvested stock options granted under the Plan.

Restricted Stock Units

During 2018 the Company granted three corporate officers restricted stock units ("RSUs") of 700,000 shares of common stock vesting over a four year period. For all RSUs, at the date of grant the recipient has all rights of a stockholder, subject to certain restrictions on transferability and a risk of forfeiture. These restricted stock grants vest in equal monthly installments from date of grant over a four year period, subject to a one-year cliff for the first vesting tranche. All restricted stock grants are approved by the Board of Directors.

The following table summarizes the Company's RSU activity for 2018:

	Number of Shares	Weighted Avg Grant Date Fair Market Value
RSUs unvested at December 31, 2017	--	\$ --
Granted during 2018	700,000	0.06
Exercised cancelled during 2018	--	--
Vested during 2018	--	--
RSUs unvested at December 31, 2018	<u>\$ 700,000</u>	<u>\$ 0.06</u>

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8. BUSINESS COMBINATIONS

In 2017, Loyyal Corporation acquired Qobolo Limited ("Qobolo"), a limited company located in the United Kingdom (subsequently renamed Loyyal UK Ltd) for the purpose of expanding operations into the United Kingdom. Qobolo was acquired for \$41,779 of Loyyal common stock.

In 2017, the Company issued Common stock as consideration for payment of the acquired subsidiary Loyyal UK Ltd. in the amount of \$41,779. In addition, see Note 1.

The following summarizes the estimated fair values of the assets and liabilities acquired at the date of acquisition:

Accounts receivable and other current assets	\$ 35,712
Property and equipment	2,043
Goodwill resulting from business combination	41,679
Accrued expenses and other current liabilities	(37,655)
	<u>\$ 41,779</u>

The goodwill arising from the acquisition consisted largely of intangible assets that do not qualify for separate recognition. The entire amount of goodwill assigned to the Company during the year presented was anticipated to be amortized and deductible for tax purposes over a period of 15 years. In 2018, the Company ceased UK operations and ultimately dissolved Qobolo resulting in a loss from discontinued operations of \$19,811.

9. RELATED PARTY TRANSACTIONS

At various points in time the Company makes loans to and receives loans from related parties for general liquidity purposes.

As of December 31, 2018, the Company had loans receivable from the founding stockholder aggregating \$100,000. The loans receivable bear interest at 2% per year and mature in 2019. Also as of December 31, 2018, the Company has loans payable to related parties, including a stockholder, in the amount of \$11,662. These loans are non-interest bearing and are payable on demand.

As of December 31, 2017, the Company had a loan due from the founding stockholder in the amount of \$3,100. The note was non-interest bearing and was repaid in 2018. Also as of December 31, 2017, the Company had loans payable to related parties, including a stockholder, in the amount of \$36,662. These loans were non-interest bearing and payable on demand.

Also, from time to time, the Company makes certain salary advances to employees or pays rental security deposits on behalf of employees to facilitate relocation. Such advances are non-interest bearing and are recorded as other current assets until repaid or forgiven.

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10. INCOME TAXES

Income tax expense (benefit) consisted of the following for the years ended December 31:

	2018	2017
Foreign taxes	\$ <u> -- </u>	\$ <u> (24,439) </u>

Deferred income tax assets consisted of the following at December 31:

	2018	2017
Deferred income tax assets	\$ 2,050,338	\$ 1,210,519
Valuation allowance	<u>(2,050,338)</u>	<u>(1,210,519)</u>
Net deferred income tax asset	<u>\$ <u> -- </u></u>	<u>\$ <u> -- </u></u>

Deferred income tax assets consist of book versus tax temporary differences relating to investments, net operating loss carry-forwards, accumulated depreciation and amortization and stock-based compensation. The Company has provided for a 100% valuation allowance for the deferred tax assets due to the uncertainty surrounding the realization of the assets.

As of December 31, 2018, the Company had federal and state net operating loss carry forwards of approximately \$7,200,000 and \$9,300,000, respectively, some of which expire at various dates through 2038.

The Tax Cuts and Jobs Act (the "Act") was enacted on December 22, 2018. The Act reduces the US federal corporate tax rate from 35% to 21%, requires companies to pay a one-time transition tax on earnings of certain foreign subsidiaries that were previously tax deferred and creates new taxes on certain foreign-sourced earnings. As of December 31, 2017, the Company has remeasured certain deferred tax assets based on the rates at which they are expected to reverse in the future, which is generally 21%.

11. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

The consolidated statements of cash flows for the years ended December 31 contain cash paid during the year for:

	2018	2017
Interest	\$ <u> 467 </u>	\$ <u> 10,889 </u>
Income taxes	<u>\$ <u> -- </u></u>	<u>\$ <u> 26,659 </u></u>

During 2017, non-cash investing and financing activities included:

- The issuance of Preferred stock for convertible debt and accrued interest in the amount of \$1,455,309.
- The issuance of Common stock in consideration for the acquisition of Qobolo in the amount of \$41,779.
- The issuance of Common stock in lieu of compensation for services in the amount of \$36,025.

12. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through August 6, 2019, the date for which the consolidated financial statements were available to be issued. Based on this evaluation, the Company identified the following subsequent events requiring disclosure within the consolidated financial statements:

- Between January and May 2019, the Company issued five “A-4 Bridge Convertible Notes” payable in the aggregate principal amount of \$720,000. The notes bear interest at 5% per annum and mature in 2020. The notes are subject to automatically convert upon equity financing. Further, if prior to the maturity date and prior to a change of control, as defined in the agreements, the Company sold or issued equity securities (other than common stock) primarily for the purpose of raising capital in one or more transactions resulting in cumulative gross proceeds to the Company equal to at least \$22,000,000, then upon the date of the closing of such equity financing, the then outstanding principal amount of the notes and all accrued interest would be automatically converted into such number of shares of the type of equity securities to be issued in the financing.
- On August 2, 2019, the Company executed a stock purchase agreement providing for the issuance and sale of up to \$3,000,000 of Series B Preferred Stock, the proceeds of which are restricted for use by the Company for general operating expenses and related activities. The Series B stock purchase agreement specifies the timeline and amount of various investment tranches and specifies the various rights, preference and privileges of the Series B Preferred Stock.