



DATATRAK International, Inc.
Quarterly Report
September 30, 2016

(OTC Pink Basic Disclosure Guidelines)

1) Name of the issuer and its predecessors (if any)

DATATRAK International, Inc. hereinafter referred to as “DATATRAK” or the “Company”.

2) Address of the issuer’s principal executive offices

Company Headquarters

5900 Landerbrook Dr.
Suite 170
Mayfield Heights, OH 44124
Phone: (440) 443-0082
Email: marketing@datatrak.com
Website: www.datatrak.com

Investor Relations Contact

Alex Tabatabai, Chairman of the Board of Directors
5900 Landerbrook Dr.
Suite 170
Mayfield Heights, OH 44124
Phone: (440) 443-0082
Email: investor@datatrak.com
Website(s): www.datatrak.com

3) Security Information

Trading Symbol: DTRK

Exact title and class of securities outstanding as of September 30, 2016:

Common Shares

The Company is authorized to issue 25,000,000 no par value Common Shares (the “Common Shares”). The Common Shares are traded through the OTC Pink Markets under the symbol “DTRK” (CUSIP 238134209). As of September 30, 2016, 1,720,842 Common Shares were outstanding.

	<u>Sep. 30, 2016</u>	<u>Dec. 31, 2015</u>
Shares authorized	25,000,000	25,000,000
Shares outstanding	1,720,842	1,514,718
No. of beneficial shareholders	Greater than 100	Greater than 100
No. of shareholders of record	66	68

Preferred Shares

The Company is authorized to issue 1,000,000 no par value Preferred Shares (the “Preferred Shares”) with such rights and preferences and in such series as determined by the Articles of Incorporation and/or the Board of Directors at the time of issuance. No Preferred Shares were issued or outstanding as of September 30, 2016.

	<u>Sep. 30, 2016</u>	<u>Dec. 31, 2015</u>
Shares authorized	1,000,000	1,000,000
Shares outstanding	-	-
No. of beneficial shareholders	-	-
No. of shareholders of record	-	-

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Transfer Agent

By Mail:

Computershare Investor Services
P.O. Box 43078
Providence, RI 02940

By Overnight Delivery:

Computershare Investor Services
250 Royall Street
Canton, MA 02021

By Telephone:

1-800-622-6757 (toll free within the United States, Canada and Puerto Rico)
1-781-575-4735 (international direct dial)

Computershare, Inc. is currently registered under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and is an authorized transfer agent subject to regulation by the U.S. Securities and Exchange Commission (the “SEC”).

List any restrictions on the transfer of security:

DATATRAK International, Inc. Common Shares are not registered with the SEC and, therefore, have a restricted legend affixed to the front of any share certificates. For non-affiliates, the restriction can be removed once the shares have been held for a period of one year.

Describe any trading suspension orders issued by the SEC in the past 12 months:

None

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization either currently anticipated or that occurred within the past 12 months:

None

4) Issuance History

As of January 1, 2014, the Company had 1,366,996 Common Shares outstanding.

The Company awarded retention bonuses to certain officers and key employees in the form of restricted stock units, which were effective after the close of business on August 16, 2011. An aggregate of 46,851 restricted stock units, with a fair value of \$330,000, were granted under the Company’s 2011 Omnibus Plan. Due to the departure of a key employee during 2013, 6,033 restricted stock units were forfeited. The remaining restricted stock units vested on January 2, 2014. The Compensation Committee of the Board of Directors decided that the restricted stock units were to be paid in Common Shares, net of applicable taxes. Therefore, only 30,141 restricted Common Shares were awarded.

On January 22, 2014, the Company made a discretionary contribution to each eligible employee’s 401(k) account in restricted Common Shares of DATATRAK’s stock with a value equal to 3% of eligible employee’s salaries, not to exceed the amount contributed by the employee. The total number of restricted shares granted in connection with such match was 14,824. The shares were issued out of the authorized but unissued share account.

On March 18, 2014, the Company made restricted share grants to certain officers and key employees in lieu of the payment of bonus amounts under the 2013 Cash Incentive Plan. Based on the closing stock price on March 18, 2014, 20,748 restricted shares were awarded to certain officers and key employees outside of the 2013 Omnibus Plan. These shares are subject to certain restrictions, including a provision that the participant’s shares shall be forfeited if such participant ceases to be employed by the Company prior to the one-year anniversary of the grant. Subsequent to the grant, a former key employee terminated employment with DATATRAK, thereby forfeiting 181 of the restricted shares granted on March 18, 2014.

The Board of Directors and the shareholders of DATATRAK International, Inc. approved the DATATRAK International, Inc. 2010 Employee Stock Purchase Plan (the “ESPP”) at the 2010 Annual Meeting. The ESPP allows employees the opportunity to purchase

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shares of *DATATRAK* stock at a 15% discounted price. The total number of shares issued out of treasury shares in connection with the ESPP in 2014 was 8,321.

As of December 31, 2014, the Company had 1,440,849 Common Shares outstanding.

On January 30, 2015, the Company made a discretionary contribution to each eligible employee's 401(k) account in restricted Common Shares of *DATATRAK*'s stock with a value equal to 3% of eligible employee's salaries, not to exceed the amount contributed by the employee. The total number of restricted shares granted in connection with such match was 20,271. The shares were issued out of the authorized but unissued share account.

On March 17, 2015, the Company made restricted share grants to certain officers and key employees in lieu of the payment of bonus amounts under the 2014 Cash Incentive Plan. Based on the closing stock price on March 17, 2015, 46,127 restricted shares were awarded to certain officers and key employees outside of the 2013 Omnibus Plan. These shares are subject to certain restrictions, including a provision that the participant's shares shall be forfeited if such participant ceases to be employed by the Company prior to the one-year anniversary of the grant.

On November 17, 2015, the Company made restricted share grants to certain employees. The restricted shares would be forfeited if the grantee's employment lapsed for any reason prior to the first anniversary of the grant date. Restricted shares totaling 47,250 were granted; however, 20,900 shares have been forfeited to date.

On November 17, 2015, the Company purportedly made restricted share grants to non-employee Directors in lieu of the payment of 75% of the quarterly cash amounts purportedly due under the Director Compensation Plan. Based on the closing stock price on November 17, 2015, 2,938 restricted shares were purportedly awarded to non-employee Directors outside of the 2013 Omnibus Plan.

The total number of shares issued out of treasury shares in connection with the ESPP in 2015 was 4,533.

As of December 31, 2015, the Company had 1,514,718 Common Shares outstanding.

On January 31, 2016, the Company made a discretionary contribution to each eligible employee's 401(k) account in restricted Common Shares of *DATATRAK*'s stock with a value equal to 3% of eligible employee's salaries, not to exceed the amount contributed by the employee. The total number of restricted shares granted in connection with such match was 36,105. The shares were issued out of the authorized but unissued share account.

The total number of shares issued out of treasury shares in connection with the ESPP in 2016 was 3,517.

On April 5, 2016, in connection with the Stock Purchase Agreement ("SPA") entered into with Tabatabai Investment Partners LP the Company agreed to issue Common Stock in exchange for receiving \$250,000 on April 8, 2016. It was also agreed that Tabatabai would cancel \$300,000 of indebtedness in exchange for a number of shares of Common Stock of *DATATRAK* equal to the amount of \$300,000 divided by the price per share equal to \$3.50. Restricted Common Shares totaling 157,142 were issued to Tabatabai Investment Partners LP based on a market price of \$3.50 under this agreement. For additional information regarding these financings, see Note 5. Recent Developments to the condensed consolidated financial statements included in this report. These financings were private placements exempt from registration under the Securities Act of 1933, as amended.

On April 12, 2016, the Company made restricted share grants to non-employee Directors in lieu of cash payments under the Director Compensation Plan for the first quarter of 2016. Based on the closing stock price on April 12, 2016, 4,341 restricted shares were awarded to non-employee Directors outside of the 2013 Omnibus Plan.

On August 5, 2016, the Company made restricted share grants to non-employee Directors under the Director Compensation Plan for the second quarter of 2016. Based on the closing stock price on August 5, 2016, 5,019 restricted shares were awarded to non-employee Directors outside of the 2013 Omnibus Plan.

As of September 30, 2016, the Company had 1,720,842 Common Shares outstanding.

All Common Shares issued by *DATATRAK* International, Inc. contain a restrictive legend since the shares are not registered with the SEC. Common Shares must be held by non-affiliates for one year for the restrictive legend to be removed. Affiliates remain subject to the restrictions under the Rule 144 promulgated under the Securities Act of 1933, as amended, as long as they are affiliates of the Company and for 90 days thereafter.

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5) Financial Statements

See the following pages for current financial information and footnotes.

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DATATRAK International, Inc.
CONDENSED CONSOLIDATED BALANCE SHEETS

	<u>September 30, 2016</u>	<u>December 31, 2015</u>
	(Unaudited)	(Note A)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 1,733,791	\$ 1,354,857
Accounts receivable, net of allowance for doubtful accounts of \$15,000 and \$15,000, respectively	715,666	895,723
Deferred tax asset – current	19,900	19,900
Deferred tax asset valuation allowance – current	(19,900)	(19,900)
Prepaid expenses	<u>242,418</u>	<u>303,171</u>
Total current assets	2,691,875	2,553,751
Property and equipment		
Equipment	370,737	448,376
Software, net of impairment	3,445,822	2,650,173
Leasehold improvements	<u>43,434</u>	<u>55,433</u>
	3,859,993	3,153,982
Less accumulated depreciation and amortization	<u>2,311,826</u>	<u>2,233,864</u>
Property and equipment, net	1,548,167	920,118
Other assets		
Certificate of deposit	301,165	300,724
Deferred tax asset – noncurrent	14,131,700	14,414,900
Deferred tax asset valuation allowance – noncurrent	(14,131,700)	(14,414,900)
Deposits	<u>11,396</u>	<u>56,975</u>
Total other assets	<u>312,561</u>	<u>357,699</u>
Total assets	<u>\$ 4,552,603</u>	<u>\$ 3,831,568</u>
LIABILITIES AND SHAREHOLDERS' DEFICIT		
Current liabilities		
Accounts payable	\$ 319,986	\$ 484,666
Notes payable – current	890,341	96,875
Accrued expenses	965,252	1,212,629
Deferred revenue	<u>1,882,896</u>	<u>3,121,597</u>
Total current liabilities	4,058,475	4,915,767
Long-term liabilities		
Long-term debt	17,631	37,647
Deferred revenue - long-term	2,668,440	3,055,826
Other long-term liabilities	<u>150,000</u>	<u>—</u>
Total long-term liabilities	2,836,071	3,093,473
Shareholders' deficit		
Serial Preferred Shares, without par value, 1,000,000 shares authorized, none issued	—	—
Common Shares/Additional paid in capital, without par value, authorized 25,000,000 shares; issued 1,734,944 shares as of September 30, 2016 and 1,532,337 as of December 31, 2015; outstanding 1,720,842 as of September 30, 2016 and 1,514,718 shares as of December 31, 2015	84,542,437	83,577,223
Treasury Shares, 14,102 shares as of September 30, 2016 at cost; 17,619 shares as of December 31, 2015 at cost	(18,501,576)	(18,515,503)
Accumulated deficit	<u>(68,382,804)</u>	<u>(69,239,392)</u>
Total shareholders' deficit	<u>(2,341,943)</u>	<u>(4,177,672)</u>
Total liabilities and shareholders' deficit	<u>\$ 4,552,603</u>	<u>\$ 3,831,568</u>

Note A: The condensed consolidated balance sheet at December 31, 2015 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

See notes to condensed consolidated financial statements.

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DATATRAK International, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenue	\$ 2,136,506	\$ 2,638,554	\$ 6,935,947	\$ 7,472,950
Direct costs	<u>391,228</u>	<u>534,375</u>	<u>1,202,674</u>	<u>1,639,434</u>
Gross profit	1,745,278	2,104,179	5,733,273	5,833,516
Selling, general and administrative expenses	1,263,371	2,318,306	4,670,252	8,367,940
Depreciation and amortization	<u>52,653</u>	<u>50,394</u>	<u>166,494</u>	<u>136,544</u>
Income (loss) from operations	429,254	(264,521)	896,527	(2,670,968)
Interest income	151	281	594	1,517
Interest expense	(15,901)	(4,186)	(23,119)	(11,609)
Loss on asset disposal	<u>(6,025)</u>	<u>—</u>	<u>(6,025)</u>	<u>—</u>
Net income (loss) before tax provision	\$ 407,479	\$ (268,426)	\$ 867,977	\$(2,681,060)
Tax provision	<u>8,802</u>	<u>—</u>	<u>11,389</u>	<u>—</u>
Net income (loss)	<u>\$ 398,677</u>	<u>\$ (268,426)</u>	<u>\$ 856,588</u>	<u>\$(2,681,060)</u>
Net income (loss) per share:				
Net income (loss) per share, basic	<u>\$ 0.23</u>	<u>\$ (0.18)</u>	<u>\$ 0.52</u>	<u>\$ (1.79)</u>
Weighted-average shares outstanding, basic	<u>1,718,932</u>	<u>1,510,577</u>	<u>1,655,044</u>	<u>1,493,848</u>
Net income (loss) per share, diluted	<u>\$ 0.22</u>	<u>\$ (0.18)</u>	<u>\$ 0.47</u>	<u>\$ (1.79)</u>
Weighted-average shares outstanding, diluted	<u>1,783,880</u>	<u>1,510,577</u>	<u>1,825,891</u>	<u>1,493,848</u>

See notes to condensed consolidated financial statements.

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DATATRAK International, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30,	
	2016	2015
Operating activities		
Net income (loss)	\$ 856,588	\$ (2,681,060)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	166,494	136,544
Stock-based compensation	287,325	145,384
Loss on disposal of equipment	6,025	—
Changes in operating assets and liabilities:		
Accrued interest income	12,867	(563)
Accounts receivable	180,057	(133,953)
Prepaid expenses	260,270	489,761
Accounts payable and accrued expenses	167,921	392,520
Deferred revenue	<u>(1,626,087)</u>	<u>658,566</u>
Net cash provided by (used in) operating activities	311,460	(992,801)
Investing activities		
Purchases of property and equipment	(6,785)	(91,111)
Capitalization of software development costs	(791,991)	(341,173)
Proceeds from the disposal of equipment	18,214	—
Net cash used in investing activities	<u>(780,562)</u>	<u>(432,284)</u>
Financing activities		
Proceeds from issuance of common stock	250,000	—
Line of credit	750,000	—
Payments of notes payable	(163,802)	(148,780)
Proceeds from ESPP	11,838	18,725
Net cash provided by (used in) financing activities	<u>848,036</u>	<u>(130,055)</u>
Increase (decrease) in cash and cash equivalents	378,934	(1,555,140)
Cash and cash equivalents at beginning of period	<u>1,354,857</u>	<u>3,510,499</u>
Cash and cash equivalents at end of period	<u><u>\$ 1,733,791</u></u>	<u><u>\$ 1,955,359</u></u>
Supplemental Schedule of Noncash Activities		
Noncash financing		
Insurance note payable	153,938	192,410
Bonuses paid in stock	—	260,621
401(k) match paid in stock	129,978	140,884
Noncash payment of debt in shares	300,000	—

See notes to condensed consolidated financial statements.

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DATATRAK International, Inc.
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT

	<u>Common Shares/Additional Paid in Capital</u>		<u>Treasury Shares</u>		<u>Accumulated Deficit</u>	<u>Total</u>
	<u>Number of Shares</u>	<u>Stated Amount</u>	<u>Number of Shares</u>	<u>Cost</u>		
Balance at January 1, 2015	1,463,001	\$82,932,715	22,152	\$(18,545,713)	\$(66,340,522)	\$(1,953,520)
Stock-based compensation	2,938	243,003		4,531		247,534
Employer Stock Purchase Plan			(4,533)	25,679		25,679
401K match...	20,271	140,884				140,884
Management bonus	46,127	260,621				260,621
Net loss					<u>(2,898,870)</u>	<u>(2,898,870)</u>
Balance at December 31, 2015	1,532,337	\$83,577,223	17,619	\$(18,515,503)	\$(69,239,392)	\$(4,177,672)
Stock-based compensation	9,360	285,236		2,089		287,325
Employee Stock Purchase Plan			(3,517)	11,838		11,838
Stock Purchase Agreement ..	157,142	550,000				550,000
401K match...	36,105	129,978				129,978
Net income					<u>856,588</u>	<u>856,588</u>
Balance at September 30, 2016	<u>1,734,944</u>	<u>\$84,542,437</u>	<u>14,102</u>	<u>\$(18,501,576)</u>	<u>\$(68,382,804)</u>	<u>\$(2,341,943)</u>

See notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of *DATATRAK* International, Inc. and subsidiaries (“*DATATRAK*” or the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information and with the guidelines from OTC Pink Markets for providing adequate current information. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The accompanying unaudited interim financial statements have been prepared by the Company’s management and independent auditors have not performed a review of these financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s Annual Report for the year ended December 31, 2015.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that might affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The Company has evaluated subsequent events through November 1, 2016. On October 21, 2016, *DATATRAK* provided its proxy materials for the 2016 Annual Meeting of Shareholders to be held on December 1, 2016. The close of business on October 3, 2016, was fixed as the record date for the determination of shareholders entitled to notice of and to vote at the Annual Meeting and any adjournments or postponements of the Annual Meeting. At the Annual Meeting, shareholders will vote upon: (1) the election of three Directors in Class II named in the Proxy Statement to hold office for two-year terms ending at the 2018 Annual Meeting of Shareholders of the Company; (2) the ratification of the appointment of Skoda Minotti & Co. as the Company’s independent auditor; and (3) such other business as may properly come before the Annual Meeting or any and all adjournments or postponements.

DATATRAK entered into an employment agreement with CEO and President, James R. Ward, effective October 1, 2016. The employment agreement provided for an annual salary of \$220,000 and an immediate equity grant of 20,000 Common Shares of the Company in consideration of his service since February 23, 2016 for \$1.00 per month. The Common Shares were granted as of the close of business on October 3, 2016 at \$7.75 per share. The employment agreement is included as an exhibit to this report.

2. Going Concern

The Company has experienced continuous net losses, negative cash flows from operations and working capital deficiencies. In order to address any working capital needs the Company may face during 2016, on April 8, 2016, *DATATRAK* entered into a convertible promissory note (“Note”) with Tabatabai Investment Partners LP, a related party, which is controlled by Mr. Tabatabai, Chairman of the Board of Directors of the Company. On August 5, 2016, the parties entered into an amendment to the Note, which changed the maximum principal amount from \$750,000 to \$1,500,000 in the aggregate. The Note provides for monthly draws on the first day of each month through March 31, 2017 when the cash balance of the Company is less than a minimum threshold amount or upon request by the Company. The maximum monthly draw is limited to the difference between the minimum threshold amount and the Company’s cash balance, or a draw by the Company of up to \$750,000, up to an aggregate of \$1,500,000 during the term of the Note. The Note carries an interest rate of twelve percent on outstanding draws and matures on June 30, 2017. At any time prior to or on the maturity date, Tabatabai Investment Partners LP has the option to convert all or any portion of the principal balance and accrued but unpaid interest then outstanding under the Note into shares of the Company’s Common Stock, calculated by dividing the amount being converted by \$3.50. As of the maturity date, the Note permits the repayment of draws and interest to be in the Company’s Common Stock at market prices, calculating the number of shares of the Company’s Common Stock to be issued by dividing the amount being converted by \$3.50. The Note includes customary default, change control and acceleration provisions. The Company made a draw under this agreement in August 2016 for \$750,000.

The Company entered into a Stock Purchase Agreement (“SPA”) with Tabatabai Investment Partners LP, to issue Company Common Stock in exchange for receiving \$250,000 on April 8, 2016. It was also agreed that Tabatabai would cancel \$300,000 of indebtedness in exchange for a number of shares of Common Stock of *DATATRAK* equal to the amount of \$300,000 divided by the price

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per share equal to \$3.50. Common Shares totaling 157,142 were issued to Tabatabai Investment Partners LP based on a market price of \$3.50 under this agreement as of April 5, 2016.

DATATRAK continuously evaluates its cost structure to timely match its cost structure with anticipated revenue and backlog. Although the Company has recently made strategic investments in its infrastructure in order to support longer-term growth, DATATRAK will continue to carefully evaluate its cost structure and implement cost cutting measures if its revenue and sales trend performance falls below its minimum expectations. In such an event, DATATRAK may also need to raise additional capital in order to fund its operations, or to cover liquidity needs beyond 2016. The Company may raise additional funds by selling debt or equity securities, by entering into strategic relationships or through other arrangements. Additional capital may not be available on acceptable terms, if at all. To the extent that additional equity capital is raised, it could have a dilutive effect on the existing shareholders.

3. Accounting Policies

Principles of Consolidation

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

Revenue Recognition and Deferred Revenue

DATATRAK recognizes revenue in accordance with SEC Staff Accounting Bulletin Topic 13, “Revenue Recognition,” and Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 605, “Revenue Recognition Multiple-Element Arrangements.” The Company recognizes revenue when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery of the product or service has occurred; the fee is fixed or determinable; and collectability is probable.

DATATRAK’s non-enterprise contracts provide a fixed price for each element to be delivered, and revenue is recognized as each multiple-element is delivered. In the case of multiple-element arrangements, the Company does enter into agreements that combine both professional services and application services. These revenues qualify as separate units of accounting in accordance with Accounting Standards Update (“ASU”) No. 2009-13 because they have value to the customer on a standalone basis. DATATRAK’s application services are frequently sold without professional services which indicate that they have standalone value. Professional services are also frequently sold separately by the Company or other vendors, which also indicate standalone value. The Company determines the price of individual elements included in multiple-element arrangements using objective, reliable evidence of fair value. This evidence is based on the vendor-specific price per element for which the Company would sell an item on a standalone basis.

DATATRAK recognizes revenue based on the performance or delivery of the following specified services or components of its contracts in the manner described below:

- Enterprise agreement revenue is recognized as services are performed, which is typically consistent with ratable recognition over the life of the contract.
- Licensing revenue (patient, points, randomization, inventory, safety case manager and user licensing) is recognized ratably over the life of the license agreement.
- Hosting revenue is recognized ratably over the term of the trial.
- Project management and data management (design, testing, quality assurance, consulting, report and export) service revenue is recognized proportionally over the life of a contract as services are performed, based on the contractual billing rate for those services.
- Data item revenue is earned based on a price per data unit as data items are entered into DATATRAK’s unified software suite.
- Classroom training services revenue is recognized as classroom training is completed, at rates based on the length of the training program.
- Internet-based training services revenue is recognized on a per user basis as self-study courses are completed and successfully passed.
- Help Desk revenue is recognized based on a monthly price per registered user or site under the contract.

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- Clinical Trial Management System revenue is recognized based on a monthly price per authorized user, clinical trial and base fee under the contract.
- Clinical Data Management revenue is recognized proportionally over the life of a contract as services are performed based on the contractual billing rate for those services.

Services provided by *DATATRAK* that are in addition to those provided for in its contracts are billed on a fee for service basis as services are completed. Costs associated with contract revenue are recognized as incurred. Costs that are paid directly by the Company's clients, and for which the Company does not bear the risk of economic loss, are excluded from revenue. The termination of a standard contract will not typically result in a material adjustment to the revenue or costs previously recognized.

Deferred revenue represents cash advances received in excess of revenue earned on contracts. Payment terms vary with each contract but may include an initial payment at the time the contract is executed, with future payments dependent upon the completion of certain contract phases or targeted milestones. In the event of contract cancellation, the Company is entitled to payment for all work performed through the point of cancellation. Likewise, in the event of contract cancellation prior to earning revenue equal to or greater than the initial payment, the Company is generally not required to refund the unused portion.

Deferred revenue not subject to potential refund as of September 30, 2016 totaled \$4,539,000. The Company's deferred revenue balance, including the long-term portion, was \$4,551,000 at September 30, 2016, of which \$12,000 was subject to refund, compared to \$6,177,000 at December 31, 2015 of which \$504,000 was subject to refund.

Concentration of Credit Risk

The Company is subject to credit risk through accounts receivable and cash equivalents. The Company does not require collateral and its accounts receivable are unsecured. The cash equivalents are placed with high credit-quality financial institutions. The Company limits the amount of credit exposure in any one institution or type of investment instrument.

Cash and cash equivalents are maintained at financial institutions and, at times, balances may exceed federally insured limits. The Company has never experienced any losses related to these balances. Interest-bearing amounts on deposit in excess of federally insured limits at September 30, 2016 and December 31, 2015 approximated \$1,484,000 and \$1,105,000, respectively.

Accounts Receivable

The Company generally invoices its customers on a monthly basis with payment terms of net 30 days from invoice date. The accounts receivable amount is recorded net of an estimated reserve for doubtful accounts. The Company has a history of favorable collections and had a reserve for uncollectible accounts of \$15,000 at September 30, 2016 and December 31, 2015, respectively. The Company's average collection period was 37 days as of September 30, 2016 compared to 41 days as of December 31, 2015. The net accounts receivable balance was \$716,000 and \$896,000 at September 30, 2016 and December 31, 2015, respectively.

Property and Equipment

Property and equipment are stated at cost. Depreciable assets consist of office and computer equipment, software and leasehold improvements. Depreciation and amortization on office and computer equipment and software are computed using the straight-line method over estimated useful lives of three to seven years. Leasehold improvements are amortized using the straight-line method over the lesser of the assets' estimated useful life or the lease term. Depreciation and amortization expense related to depreciable assets, including assets recorded under capital leases, was \$53,000 and \$50,000 for quarter ended September 30, 2016 and 2015, respectively. During the nine months ended September 30, 2016, \$166,000 of depreciation and amortization expense was recorded compared to \$137,000 for the nine months ended September 30, 2015.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB ASC 718, "*Stock Compensation*," using the "modified prospective" method. On May 14, 2013, the Company's Board of Directors approved the 2013 Omnibus Equity Plan ("2013 Omnibus Plan"), thereby replacing the 2011 Omnibus Equity Plan ("2011 Omnibus Plan") as the primary share-based incentive award program for covered employees and directors. The 2011 Omnibus Plan was the primary share-based incentive award program from its approval on August 10, 2011 until the approval of the 2013 Omnibus Plan. Prior to the 2011 Omnibus Plan, the 2009 Omnibus Equity Plan (the "2009 Omnibus Plan") was the Company's primary share-based incentive award program for covered

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employees and directors from its approval on August 26, 2009 until the approval of the 2011 Omnibus Plan. Common Share options have been awarded under the 2013 Omnibus Plan, the 2011 Omnibus Plan and the 2009 Omnibus Plan. The Company used the Black-Scholes option valuation model to calculate the fair value of stock options granted.

Common Shares and Common Share options awarded to non-employee Directors are fully vested and compensation costs are completely expensed on the grant date. Compensation expense for share-based incentive awards granted to employees vest over the assigned vesting period and related compensation costs are amortized ratably over the vesting period. Stock compensation expense was \$53,000 and \$46,000 for the quarter ended September 30, 2016 and 2015, respectively. For the nine months ended September 30, 2016, stock compensation expense was \$287,000 compared to \$145,000 for the nine months ended September 30, 2015. The year-over-year increase in expense was due to the accelerated vesting of certain stock options issued under the 2013 Omnibus Plan and restricted stock awards granted to certain employees in November 2015. The 2013 Omnibus Plan was amended on December 29, 2015 to include a change in control clause that was actuated with the board resignations in February 2016. The current Board of Directors expects that it will challenge the validity and/or enforceability of the amendment. The Company's unamortized compensation cost, related to non-vested stock options and restricted Common Shares, at September 30, 2016 and 2015 was \$23,000 and \$227,000, respectively. The unamortized cost of \$23,000 at September 30, 2016 is expected to be amortized in the amounts of \$3,000, \$12,000 and \$8,000 in 2016, 2017 and 2018, respectively.

Income Taxes

The Company follows FASB ASC 740. This accounting standard requires that the liability method be used in accounting for income taxes. Under this accounting method, deferred tax assets and liabilities are determined based on the differences between the financial reporting basis and the tax basis of assets and liabilities and are measured using the enacted tax rates and laws that apply in the periods in which the deferred tax asset or liability is expected to be realized or settled. A valuation allowance is provided for deferred tax assets for which realization currently is not more likely than not. Quarterly income taxes are recorded at the effective rate, based on annual forecasted income. The Company currently is in an overall cumulative loss position totaling approximately \$40 million. As a result, the Company recorded a full valuation reserve against its net deferred tax assets in 2009 and the full valuation reserve remained on the books through September 30, 2016. However, due to effect of Alternative Minimum Tax ("AMT"), the Company recorded a tax provision of \$11,400 as of September 30, 2016. There was no provision necessary for the previous year.

In accordance with FASB ASC 740-10, the Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likelihood of being recognized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. As of September 30, 2016 and 2015, the Company had no uncertain income tax positions.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that might affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Financial Instruments

The carrying values of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses are reasonable estimates of fair value due to the short-term nature of these financial instruments.

Advertising Costs

Advertising costs are expensed as incurred and are included in selling, general and administrative expenses. Advertising costs were \$28,000 and \$86,000 for the quarter ended September 30, 2016 and 2015, respectively. For the nine months ended September 30, 2016 advertising costs totaled \$150,000 compared to \$318,000 for the nine months ended September 30, 2015. The year-over-year decrease was due to less trade show attendance and a re-evaluation of previously used advertising methods to ensure a higher rate of return.

Software Development Costs

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Development costs incurred in the research and development of new software products, enhancements to existing software products and maintenance activities are accounted for in accordance with FASB ASC 350-40, “*Accounting for Cost of Internal-Use Software, Including Enterprise Software.*” Post-implementation stage activities such as maintenance or modifications that do not result in additional functionality are expensed as incurred. Enhancements to the software, which enable the software to perform tasks that it was previously incapable of performing, are to be capitalized based on the assigned fair value. If the project contains both elements of upgrades that provide additional functionality and maintenance, cost is allocated based on relative fair values. If the cost cannot be allocated between maintenance and upgrades on a reasonable basis, all cost is expensed as incurred.

The Company capitalized software development costs that provided additional functionality of \$296,000 during the quarter ended September 30, 2016 compared to \$171,000 for the quarter ended September 30, 2015. During the nine months ended September 30, 2016 and 2015, software development costs of \$792,000 and \$341,000, respectively, were capitalized in accordance with FASB ASC 350-40.

Research and development expenses included in selling, general and administrative expenses were \$149,000 and \$271,000 for the quarters ended September 30, 2016 and 2015, respectively. Research and development expenses included in selling, general and administrative expenses were \$574,000 and \$996,000 for the nine months ended September 30, 2016 and 2015, respectively.

Subsequent Events

The Company has evaluated subsequent events through November 1, 2016. On October 21, 2016, DATATRAK provided its proxy materials for the 2016 Annual Meeting of Shareholders to be held on December 1, 2016. The close of business on October 3, 2016, was fixed as the record date for the determination of shareholders entitled to notice of and to vote at the Annual Meeting and any adjournments or postponements of the Annual Meeting. On the record date, 1,745,293 Common Shares were outstanding and entitled to vote. Each Common Share is entitled to one vote. At the Annual Meeting, shareholders will vote upon: (1) the election of three Directors in Class II named in the Proxy Statement to hold office for two-year terms ending at the 2018 Annual Meeting of Shareholders of the Company; (2) the ratification of the appointment of Skoda Minotti & Co. as the Company’s independent auditor; and (3) such other business as may properly come before the Annual Meeting or any and all adjournments or postponements.

DATATRAK entered into an employment agreement with CEO and President, James R. Ward, effective October 1, 2016. The employment agreement provided for an annual salary of \$220,000 and an immediate equity grant of 20,000 Common Shares of the Company in consideration of his service since February 23, 2016 for \$1.00 per month. The Common Shares were granted as of the close of business on October 3, 2016 at \$7.75 per share. The employment agreement is included as an exhibit to this report.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation.

4. Recently Issued Accounting Standards

In June 2016, the FASB issued ASU No. 2016-13, “*Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,*” which amends the impairment model by requiring entities to use a forward-looking approach based on expected losses to estimate credit losses on certain types of financial instruments, including trade receivables. The ASU is effective for public entities for fiscal years beginning after December 15, 2019, with early adoption permitted. Management has not yet completed its assessment of the impact of the new standard on the Company’s consolidated financial statements.

In August 2016, FASB issued ASU 2016-15, “*Classification of Certain Cash Receipts and Cash Payments.*” ASU 2016-15 clarifies how certain cash receipts and cash payments are presented in the statement of cash flows. The amendments are intended to reduce diversity in practice. The Company does not expect the adoption of ASU 2016-15 to have a material impact on the consolidated financial statements.

5. Recent Developments

On May 18, 2016, DATATRAK entered into an employment agreement with CFO Julia Henderson. The employment agreement provided for an annual salary of \$140,000 and is included as an exhibit to this report.

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On July 7, 2016 the Company entered into a sublease agreement with OERM Software, Inc., now known as Sphera Solutions, Inc., for the Chicago, IL office space ("Chicago sublease"). The Chicago sublease covers the remaining term of the original lease. Further information is included in Note 7.

On August 5, 2016, the Board of Directors appointed Mr. Eric J. Wilhelm as a Class II director with a term expiring at the 2016 annual meeting of shareholders or until his successor is duly elected and qualified, subject to his earlier death, retirement, resignation or removal.

On August 5, 2016, DATATRAK and Tabatabai Investment Partners LP entered into the first amendment to the convertible promissory note ("Note") originally entered into on April 8, 2016. The note was amended to change the maximum principal amount from \$750,000 to \$1,500,000, in aggregate. The note was further amended to allow the Company to request a draw up to \$750,000. The Company requested and received a draw of \$750,000 in August 2016.

6. Net Income (Loss) per Share

The following table sets forth the computation of basic and diluted net income (loss) per share:

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2016</u>	<u>2015</u>	<u>2016</u>	<u>2015</u>
Net income (loss) used in the calculation of basic and diluted income (loss) per share	\$ 399,000	\$ (268,000)	\$ 857,000	\$ (2,681,000)
Denominator for basic net income (loss) per share — weighted-average common shares outstanding	1,719,000	1,511,000	1,655,000	1,494,000
Effect of dilutive common share options	65,000	—	171,000	—
Denominator for diluted net income (loss) per share	<u>1,784,000</u>	<u>1,511,000</u>	<u>1,826,000</u>	<u>1,494,000</u>
Basic net income (loss) per share	\$ 0.23	\$ (0.18)	\$ 0.52	\$ (1.79)
Diluted net income (loss) per share	\$ 0.22	\$ (0.18)	\$ 0.47	\$ (1.79)
Weighted-average common share options excluded from the computation of diluted net income (loss) per share because they would have an anti-dilutive effect on net income (loss) per share	22,000	81,000	133,000	81,000

7. Operating Leases

The Company leases certain office equipment and space, some of which are under month-to-month agreements. On July 7, 2016, the Company entered into a sublease agreement with OERM Software, Inc., now known as Sphera Solutions, Inc., for the Chicago, IL office space ("Chicago sublease"). The Chicago sublease covers the remaining term of the original lease.

Net rent expense relating to the operating leases was approximately \$40,000 and \$149,000 for the quarters ended September 30, 2016 and 2015, respectively. For the nine months ended September 30, 2016 and 2015, rent expense was \$360,000 and \$411,000, respectively. Future minimum lease payments for the Company under non-cancelable operating leases as of September 30, 2016 are as follows:

<u>Year Ending September 30,</u>	<u>Amount*</u>
2017.....	\$ 537,000
2018.....	443,000
2019.....	544,000
2020.....	551,000
2021 and remainder.....	3,157,000
Total	<u>\$ 5,232,000</u>

* DATATRAK remains responsible for the master lease for the Chicago office space. The master lease contains material monthly escalation costs of \$19,300, which are included in the future minimum lease payments above.

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Future minimum lease payments expected to be received under the Chicago sublease agreement are as follows:

<u>Year Ending September 30,</u>	<u>Amount</u>
2017	\$ 298,000
2018	453,000
2019	461,000
2020	468,000
2021 and remainder.....	2,700,000
Total	<u>\$ 4,380,000</u>

8. Income Taxes

Due to its net operating loss carryforwards, the Company had no state or local income tax expense for the three and nine months ended September 30, 2016 and 2015. However, due to AMT limitations on the use of net operating loss carryforwards, *DATATRAK* recorded \$8,800 and \$11,400 of federal income tax expense for the three months and nine months ended September 30, 2016, respectively. No federal income tax was recorded for the three months and nine months ended September 30, 2015.

A reconciliation of income tax expense (benefit) at the U.S. federal statutory rate to the effective income tax rate is as follows:

	<u>Nine Months Ended September 30,</u>	
	<u>2016</u>	<u>2015</u>
Income tax expense (benefit) at the United States statutory rate	\$ 295,000	\$ (911,000)
Change in valuation allowance	(283,000)	888,000
Net operating loss adjustments	(4,000)	7,000
Non-deductible permanent differences	3,000	16,000
	<u>\$ 11,000</u>	<u>\$ —</u>

9. Long-Term Debt

Long-term debt at September 30, 2016 and December 31, 2015 is summarized below:

	<u>2016</u>	<u>2015</u>
Capital lease agreement with Dell Financial Services, LLC	\$ 51,000	\$ 90,000
Oracle note payable	—	6,000
De Lage Landen note payable	15,000	—
Insurance note payable	79,000	39,000
Tabatabai Investment, Ltd. promissory note	<u>763,000</u>	<u>—</u>
Total debt	908,000	135,000
Less current maturities	<u>(890,000)</u>	<u>(97,000)</u>
Long-term debt	<u>\$ 18,000</u>	<u>\$ 38,000</u>

The Dell Financial Services, LLC Agreements were for the purchase of certain computer equipment. The terms of the lease agreements require *DATATRAK* to make 36 monthly payments, including accrued interest, in the following amounts: \$650 beginning in December 2013 and ending in November 2016; \$537 beginning in January 2014 and ending in December 2016; \$2,760 beginning in November 2014 and ending in September 2017; \$291 beginning in June 2015 and ending in May 2018; and \$586 beginning in July 2015 and ending in June 2018. All leases include bargain purchase options at the end of the lease term.

The Company entered into a financing agreement with Oracle Credit Corporation for payment of the Company's Oracle licensing and support premiums. The note bore interest at 21.9% and was due in four quarterly installments of \$2,000, including accrued interest, beginning in January 2016 and ending in August 2016.

The Company entered into a financing agreement with De Lage Landen Financial Services for the purchase of certain office equipment. The note bears interest at 6.7% and is due in monthly installments of \$396, including accrued interest, beginning in May 2015 and ending in May 2020.

The Company entered into a financing agreement with AFCO for payment of a portion of the Company's annual insurance premiums. The note bears interest at 3.45% and is due in monthly installments of \$15,992, including accrued interest, beginning in May 2016 and ending in February 2017.

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On August 5, 2016, *DATATRAK* and Tabatabai Investment Partners LP entered into the first amendment to the convertible promissory note (“Note”) originally entered into on April 8, 2016. The note was amended to change the maximum principal amount from \$750,000 to \$1,500,000, in aggregate. The note was further amended to allow the Company to request a draw up to \$750,000. The Company requested and received a draw of \$750,000 in August 2016. The Note carries an interest rate of twelve percent on outstanding draws and matures on June 30, 2017. At any time prior to or on the maturity date, Tabatabai Investment Partners LP has the option to convert all or any portion of the principal balance and accrued but unpaid interest then outstanding under the Note into shares of the Company’s Common Stock, calculated by dividing the amount being converted by \$3.50. As of the maturity date, the Note permits the repayment of draws and interest to be in the Company’s Common Stock at market prices, calculating the number of shares of the Company’s Common Stock to be issued by dividing the amount being converted by \$3.50. The Note includes customary default, change control and acceleration provisions.

10. Software Development Costs

Development costs incurred in the research and development of new software products, enhancements to existing software products and maintenance activities are accounted for in accordance with FASB ASC 350-40, “*Accounting for Cost of Internal-Use Software, Including Enterprise Software.*” Post-implementation stage activities such as maintenance or modifications that do not result in additional functionality are expensed as incurred. Enhancements, which enable the software to perform tasks that it was previously incapable of performing, are to be capitalized based on the assigned fair value. If the project contains both elements of upgrades that provide additional functionality and maintenance, cost is allocated based on relative fair values. If the cost cannot be allocated between maintenance and upgrades on a reasonable basis, all cost is expensed as incurred.

The Company’s software development costs generally contain both upgrades that provided additional functionality and maintenance items. During the quarter ended September 30, 2016 and 2015, software development costs of \$296,000 and \$171,000, respectively, were capitalized in accordance with FASB ASC 350-40. During the nine months ended September 30, 2016 and 2015, software development costs of \$792,000 and \$341,000, respectively, were capitalized in accordance with FASB ASC 350-40. Capitalized software development costs are amortized over 36 months starting when the enhancements are placed in service.

Research and development expenses included in selling, general and administrative expenses were \$149,000 and \$271,000 for the quarters ended September 30, 2016 and 2015, respectively. Research and development expenses included in selling, general and administrative expenses were \$574,000 and \$996,000 for the nine months ended September 30, 2016 and 2015, respectively.

11. Contingencies

On November 10, 2015, *DATATRAK* postponed the annual shareholder meeting schedule for November 11, 2015 and under the direction of the previous Board initiated a lawsuit against Alex Tabatabai and Arosa Investment Management, LLC (collectively, “Arosa”). (See Case No. CV-15-854059, Cuyahoga County, Ohio Common Pleas Court). *DATATRAK* asserted various claims in connection with Arosa’s proxy contest involving three seats on the *DATATRAK* Board of Directors. On November 25, 2015, Arosa asserted counterclaims and individual and shareholder derivative third-party claims against *DATATRAK* and five then *DATATRAK* directors, Laurence P. Birch, Timothy G. Biro, James M. Karis, Jerome H. Kaiser and Nicholas A. Loiacono, as well as Andrew T. Pitler, who Arosa claimed was unlawfully appointed to *DATATRAK*’s board, and direct claims against *DATATRAK* and Mr. Birch. Arosa asserted various claims of unlawfully delaying the Board of Directors election that Arosa’s slate of director candidates had won going into the scheduled November 11, 2015 annual shareholder meeting.

On January 8, 2016, the 2015 *DATATRAK* annual shareholders’ meeting was held following two postponements, and Arosa’s slate prevailed by receiving approximately 62% of shareholder votes cast. Following the election, Arosa, Tabatabai, *DATATRAK*, Biro, Karis, Kaiser, Loiacono, and Pitler (collectively, the “Settling Parties”) commenced settlement discussions in an effort to avoid additional litigation expenses. As a result of these discussions, Kaiser, Karis, and Pitler agreed to resign from *DATATRAK*’s Board of Directors and Arosa agreed to a mutual release and dismissal with prejudice of all claims among the Settling Parties. None of the Settling Parties made any payment as part of the settlement.

On March 4, 2016, the Court granted a preliminary order to approve the proposed settlement agreement. The preliminary order required the parties to provide notice of the proposed settlement agreement to all *DATATRAK* shareholders, and provide shareholders with time to object. The Court received two objections. One was from a shareholder and the other was from Mr. Birch, who was terminated as CEO on February 23, 2016. On March 16, 2016, Birch filed a fourth-party complaint against *DATATRAK*, alleging a breach of contract claim against *DATATRAK* related to his employment agreement. On March 25, 2016, Birch amended his fourth-party complaint to add an indemnification claim against *DATATRAK*. On April 22, 2016, *DATATRAK* responded to Birch’s fourth-party

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complaint, denying the allegations asserted against it, and asserting a counterclaim against Birch, alleging claims for declaratory judgment, fraud, unjust enrichment, breach of the implied covenant of good faith and fair dealing, breach of fiduciary duty, and a claim under the faithless servant doctrine that Birch breached the implied condition of employment that he would carry out his duties in good faith and not act to the detriment of *DATATRAK*. On June 30, 2016, the Court issued an order requiring the settling parties to submit a revised notice of the proposed settlement for the Court's consideration to clarify that the claims by and against Birch would not be covered by the proposed settlement, the impact of the proposed settlement regarding the released directors, and the parties' positions with regard to indemnification. On August 15, 2016, the settling parties submitted the revised proposed notice. The Court then directed the parties to consider whether mediation may assist the parties in reaching a global resolution of all claims in the dispute. Further proceedings on approval of the revised proposed notice to shareholders and approval of the proposed settlement are currently stayed pending a determination as to whether mediation as to the claims by and against Birch will be pursued.

On May 27, 2016, former CFO Jennifer Mabe and former VP Legal Varnesh Sritharan filed a lawsuit against *DATATRAK* in the United States District Court for the Northern District of Ohio, Case No. 1:16 CV 01286, alleging claims for breach of contract related to their employment agreements, retaliation in violation of the Sarbanes Oxley Act, defamation and wrongful termination in violation of public policy. On August 24, 2016, *DATATRAK* filed a motion to dismiss the retaliation in violation of the Sarbanes Oxley Act, defamation and wrongful termination in violation of public policy claims; filed an answer denying the substance of the remaining claims; and filed a counterclaim against Ms. Mabe and Mr. Sritharan, alleging claims for declaratory judgment, breach of the implied covenant of good faith and fair dealing, breach of fiduciary duty, and a claim under the faithless servant doctrine that they breached the implied condition of employment that they would carry out their duties in good faith and not act to the detriment of *DATATRAK*. On September 13, 2016, Ms. Mabe and Mr. Sritharan filed a first amended complaint. On September 27, 2016, *DATATRAK* filed a motion to dismiss, answer, and counterclaim in response to the first amended complaint. The Company believes the claims asserted by Ms. Mabe and Mr. Sritharan are without merit and intends to vigorously defend the same.

In addition to the foregoing, in the ordinary course of business, the Company is involved in ordinary, routine legal proceedings. Additionally, certain of the Company's revenues may be subject to sales and use tax in certain jurisdictions. The Company has assessed its positions and is of the opinion that the ultimate resolution of such matters will not have a material adverse effect on the results of operations, cash flows or the financial position of the Company.

12. Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

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6) Describe the Issuer's Business, Products and Services

A. Description of the issuer's business operations:

DATATRAK International, Inc. ("DATATRAK" or the "Company") is one of the first and leading technology and services company delivering global *unified dClinical*[™] solutions for the clinical trials industry, including electronic data capture ("EDC") and clinical trial management software ("CTMS") solutions. DATATRAK provides clinical enterprise solutions to safely accelerate every drug, every biologic and every device *from Concept to Cure*[®]. Customers use DATATRAK software to collect, review, transfer and store clinical trial data electronically in a secure environment. DATATRAK customers are companies in the pharmaceutical, biotechnology, contract research organization ("CRO"), academic research organization ("ARO") and medical device industries. The Company's services support clients in accelerating the completion of clinical research more efficiently and safely by providing improved data quality and real time access to information on a global scale.

Enhancements are routinely made to the DATATRAK unified platform, which continue to simplify the management of data for clinical research. In addition, extensive work has been completed for the 2016 release of UX CTMS 360[™], the development of which was directed by members of the Company's Product Advisory Council ("PAC"). The system is deployed worldwide as Software as a Service ("SaaS") through the cloud and supports pre-clinical and Phase I – Phase IV drug and device studies in multiple languages throughout the world. DATATRAK delivers a *unified dClinical*[®] platform that leverages the power of single database architecture, removing complexities in clinical research to deliver time and cost savings.

Financial Performance

The Company's revenue decreased \$537,000, from \$7,473,000 for the nine months ended September 30, 2015 to \$6,936,000 for the nine months ended September 30, 2016. The revenue decline was mainly due to revenue from new contract sales but the Company also saw a decrease in revenue from contracts in backlog due to lower change orders and contract expansions. The decrease in revenue from new contract sales was due to the Company falling short of its sales goals during the latter half of 2015 and for the first half of 2016. It is no secret that the sales effort was challenged during this time period due to a depleted sales team and the leadership transition. DATATRAK has planned changes to its product offering, pricing and contracting process which it believes will lead to stronger customer relationships through greater transparency and help to build future revenue. Direct costs decreased by 27% during this same time period due to lower employee costs. The Company's gross margin was 83% for the nine months ended September 30, 2016 compared to 78% for the nine months ended September 30, 2015. SG&A expenses decreased by \$3,698,000, or 44%, for the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015. The decrease was primarily due to lower employee costs, including bonus, recruitment and travel. The Company also cut spending for advertising, equipment and legal. The first nine months of 2015 included substantial expenses related to the patent defense litigation, which was settled in early 2016. As a result, DATATRAK had income from operations for the nine months ended September 30, 2016 of \$897,000 compared to a loss from operations of \$(2,671,000) for the nine months ended September 30, 2015.

Backlog

Backlog consists of future value from authorization letters to commence services, statements of work, technology and services agreements, change orders and other customer contracts, billed and unbilled. At September 30, 2016, the Company's backlog decreased by 13%, to \$23,321,000 from \$26,682,000 at December 31, 2015. The decrease in backlog was due to lower new contract sales during the first nine months of 2016.

All contracts are subject to possible delays or cancellation or can change in scope in a positive or negative direction. Approximately 85% of the Company's September 30, 2016 backlog is subject to being cancelled or delayed at any time. Therefore, current backlog is not necessarily indicative of the Company's future quarterly or annual revenue. Historically, backlog has not always been an accurate predictor of the Company's short-term revenue.

Results of Operations

Three months ended September 30, 2016 compared with the three months ended September 30, 2015

Revenue for the three months ended September 30, 2016 decreased by 19% to \$2,137,000 as compared to \$2,639,000 for the three months ended September 30, 2015. During the third quarter of 2016, DATATRAK recorded revenue related to 122 contracts compared to 136 contracts during the third quarter of 2015. For the three months ended September 30, 2016, \$1,882,000 of revenue was the result of contracts that were in backlog at December 31, 2015 and \$255,000 was the result of new business signed since January 1,

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2016. For the three months ended September 30, 2015, \$1,946,000 of revenue was generated from contracts that were in backlog at December 31, 2014 and \$693,000 was the result of new business signed since January 1, 2015.

The Company recorded \$1,036,000 in revenue during the three months ended September 30, 2016 compared to \$937,000 during the three months ended September 30, 2015 from significant multi-year enterprise license agreements. The Company will continue to recognize the remaining, non-refundable, aggregate deferred revenue on the enterprise license agreements ratably, or in line with the acceleration of points contained in the license agreement, over the remaining lives of each respective license period. The enterprise license agreements totaled \$28.1 million of original contract value.

Direct costs of revenue decreased 27%, from \$534,000 for the three months ended September 30, 2015, to \$391,000 for the three months ended September 30, 2016. The \$143,000 decrease was due to lower employee costs, but was partially offset by higher internet service provided ("ISP") costs. Certain expenses were reclassified during 2016 to more accurately reflect ISP costs. The Company's gross margin was 82% for the three months ended September 30, 2016 compared to 80% for the three months ended September 30, 2015.

SG&A expenses include all administrative personnel costs, sales and software development costs, stock compensation and all other expenses not directly chargeable to a specific contract. SG&A expenses decreased by \$1,055,000, or 46%, to \$1,263,000 from \$2,318,000 for the three months ended September 30, 2016 and 2015, respectively. The decrease was primarily due to lower employee costs, including bonus, recruitment and travel. Rent expense decreased for the quarter due to the assignment of the North Carolina office and the sublease of the Chicago office; however, consulting costs increased for the quarter due to the broker fee incurred in connection with the Chicago sublease. The Company also cut spending for advertising, equipment and legal.

Depreciation and amortization expense increased by \$3,000 from \$50,000 for the three months ended September 30, 2015 to \$53,000 for the three months ended September 30, 2016.

Non-cash charges were \$112,000 for the three months ended September 30, 2016 compared to \$97,000 for the three months ended September 30, 2015. The increase in non-cash charges was due to a loss on disposal of equipment, depreciation and stock compensation.

Nine months ended September 30, 2016 compared with the nine months ended September 30, 2015

Revenue for the nine months ended September 30, 2016 decreased by 7% to \$6,936,000 as compared to \$7,473,000 for the nine months ended September 30, 2015. During the first nine months of 2016, DATATRAK recorded revenue related to 148 contracts compared to 158 contracts during the first nine months of 2015. For the nine months ended September 30, 2016, \$6,359,000 of revenue was the result of contracts that were in backlog at December 31, 2015 and \$577,000 was the result of new business signed since January 1, 2016. For the nine months ended September 30, 2015, \$6,529,000 of revenue was generated from contracts that were in backlog at December 31, 2014 and \$944,000 was the result of new business signed since January 1, 2015.

The Company recorded \$3,356,000 in revenue during the nine months ended September 30, 2016 compared to \$2,508,000 during the nine months ended September 30, 2015 from significant multi-year enterprise license agreements. The Company will continue to recognize the remaining, non-refundable, aggregate deferred revenue on the enterprise license agreements ratably, or in line with the acceleration of points contained in the license agreement, over the remaining lives of each respective license period. The enterprise license agreements totaled \$28.1 million of original contract value.

Direct costs of revenue decreased 27%, from \$1,639,000 for the nine months ended September 30, 2015, to \$1,203,000 for the nine months ended September 30, 2016. The \$436,000 decrease was due to lower employee costs, but was partially offset by higher internet service provided ("ISP") costs. Certain expenses were reclassified during 2016 to more accurately reflect ISP costs. The Company's gross margin was 83% for the nine months ended September 30, 2016 compared to 78% for the nine months ended September 30, 2015.

SG&A expenses include all administrative personnel costs, sales and software development costs, stock compensation and all other expenses not directly chargeable to a specific contract. SG&A expenses decreased by \$3,698,000, or 44%, to \$4,670,000 from \$8,368,000 for the nine months ended September 30, 2016 and 2015, respectively. The decrease was primarily due to lower employee costs, including bonus, recruitment and travel. Rent expense decreased due to the assignment of the North Carolina office and the sublease of the Chicago office. The Company also cut spending for advertising, equipment and legal. Included in SG&A costs for the nine months ended September 30, 2016 was \$300,000 of indebtedness for legal fees owed to Tabatabai Investment Partners LP that

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was cancelled in exchange for shares of the Company's Common Stock. The first nine months of 2015 included substantial expenses related to the patent defense litigation, which was settled in early 2016.

Depreciation and amortization expense increased by \$30,000 from \$137,000 for the nine months ended September 30, 2015 to \$167,000 for the nine months ended September 30, 2016. The increase was due to the capitalization of software development costs and assets purchased or acquired through capital leases.

Non-cash charges were \$460,000 for the nine months ended September 30, 2016 compared to \$282,000 for the nine months ended September 30, 2015. The year-over-year increase in non-cash charges was due to depreciation, which was caused by more asset purchases and capitalization of software development, higher stock compensation due to the purported amendment of the 2013 Omnibus Plan which accelerated the vesting of certain stock options and the loss on asset disposal.

Liquidity and Capital Resources

The Company's principal sources of cash are existing cash and cash flow from operations. Contracts with customers usually require a portion of the contract amount to be paid at the time the contract is initiated. Additional payments are generally received monthly as work on the contract progresses. The Company records all amounts received as a liability (deferred revenue) until work has been completed and revenue is recognized. Cash receipts do not necessarily correspond to costs incurred or revenue recognized. DATATRAK's primary cash needs are to fund normal working capital requirements.

On April 8, 2016, DATATRAK entered into a convertible promissory note ("Note") with Tabatabai Investment Partners LP, a related party, which is controlled by Mr. Tabatabai, Chairman of the Board of Directors of the Company. On August 5, 2016, the parties entered into an amendment to the Note, which changed the maximum principal amount from \$750,000 to \$1,500,000 in the aggregate. The Note provides for monthly draws on the first day of each month through March 31, 2017 when the cash balance of the Company is less than a minimum threshold amount or upon request by the Company. The maximum monthly draw is limited to the difference between the minimum threshold amount and the Company's cash balance, or a draw by the Company of up to \$750,000, up to an aggregate of \$1,500,000 during the term of the Note. The Note carries an interest rate of twelve percent on outstanding draws and matures on June 30, 2017. At any time prior to or on the maturity date, Tabatabai Investment Partners LP has the option to convert all or any portion of the principal balance and accrued but unpaid interest then outstanding under the Note into shares of the Company's Common Stock, calculated by dividing the amount being converted by \$3.50. As of the maturity date, the Note permits the repayment of draws and interest to be in the Company's Common Stock at market prices, calculating the number of shares of the Company's Common Stock to be issued by dividing the amount being converted by \$3.50. The Note includes customary default, change control and acceleration provisions. The Company made a draw under this agreement in August 2016 for \$750,000.

The Company entered into a Stock Purchase Agreement ("SPA") with Tabatabai Investment Partners LP, to issue Company Common Stock in exchange for receiving \$250,000 on April 8, 2016. It was also agreed that Tabatabai would cancel \$300,000 of indebtedness in exchange for a number of shares of Common Stock of DATATRAK equal to the amount of \$300,000 divided by the price per share equal to \$3.50. Common Shares totaling 157,142 were issued to Tabatabai Investment Partners LP based on a market price of \$3.50 under this agreement as of April 5, 2016.

Cash Flow

A summary of operating, investing and financing cash flow activities are shown in the following table for the nine months ended September 30, 2016 and 2015 (rounded to the nearest thousand):

	<u>Nine Months Ended September 30,</u>	
	<u>2016</u>	<u>2015</u>
Cash Flow Summary:		
Provided by (used in) operating activities	\$ 312,000	\$ (993,000)
Used in investing activities	(781,000)	(432,000)
Provided by (used in) financing activities	<u>848,000</u>	<u>(130,000)</u>
Increase (decrease) in cash and cash equivalents	<u>\$ 379,000</u>	<u>\$ (1,555,000)</u>
Cash balance at beginning of period	<u>1,355,000</u>	<u>3,510,000</u>
Cash balance at end of period	<u>\$ 1,734,000</u>	<u>\$ 1,955,000</u>

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The Company's net cash flow from operations was \$312,000 for the nine months ended September 30, 2016 compared to \$(993,000) for the nine months ended September 30, 2015. The \$1,305,000 increase in cash flow from operations was primarily due to the \$3,538,000 change in the net income during the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015, which was caused by a significant reorganization that took place during the first quarter of 2016. Operating assets and liabilities decreased by \$(2,411,000) during the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015 mainly due to the decrease in deferred revenue and accrued expense changes year-over-year. The net cash flow from operations was positively impacted by a \$178,000 increase in non-cash items, which includes depreciation, stock compensation expense and loss on asset disposal, from the nine months ended September 30, 2015 to the nine months ended September 30, 2016.

The Company's net cash flow from investing activities was \$(781,000) compared to \$(432,000) due to the capitalization of software development costs and the purchase of assets during the nine months ended September 30, 2016 and 2015, respectively. The nine months ended September 30, 2016 included \$18,000 of proceeds from the disposal of equipment that was sold as part of the Chicago sublease.

Net cash of \$848,000 was provided by financing activities for the nine months ended September 30, 2016 compared to \$(130,000) used during the nine months ended September 30, 2015. Financing activities for the nine months ended September 30, 2016 included cash outlays of \$(164,000) for the repayment of capital lease related debt and notes payable, which was offset by cash inflows of \$250,000 received in connection with the SPA, \$12,000 from the Employee Stock Purchase Plan and \$750,000 drawn on the Tabatabai promissory note. In the nine months ended September 30, 2015, \$(149,000) was used for the repayment of capital lease related debt and notes payable, which was partially offset by the \$19,000 inflow from the Employee Stock Purchase Plan.

As a result of the changes above, the cash balance at September 30, 2016 was \$1,734,000 compared to \$1,955,000 at September 30, 2015.

DATATRAK's "days sales outstanding" was 37 days at September 30, 2016 compared to 41 days at December 31, 2015. Trade accounts receivable (net of allowance for doubtful accounts of \$15,000) was \$716,000 at September 30, 2016 and \$896,000 at December 31, 2015.

Management believes DATATRAK will have available funds in order to meet its short-term working capital requirements for at least the next 12 months. However, it must be noted that the prior board and former CEO did spend a significant amount of the Company's assets on delaying and attempting to win the recent shareholder director election and on other non-recurring events such as the patent litigation and the investigation of the former CEO and his alleged misconduct. At September 30, 2016, the Company had working capital of \$(1,367,000) compared to working capital of \$(2,362,000) as of December 31, 2015. In order to address any working capital needs the Company may face during 2016, on April 8, 2016, DATATRAK entered into a convertible promissory note ("Note") with Tabatabai Investment Partners LP, a related party, which is controlled by Mr. Tabatabai, Chairman of the Board of Directors of the Company. On August 5, 2016, the parties entered into an amendment to the Note, which changed the maximum amount from \$750,000 to \$1,500,000 in the aggregate. The Note provides for monthly draws on the first day of each month through March 31, 2017 when the cash balance of the Company is less than a minimum threshold amount or upon request by the Company. The maximum monthly draw is limited to the difference between the minimum threshold amount and the Company's cash balance, or a draw by the Company of up to \$750,000, up to an aggregate of \$1,500,000 during the term of the Note. The Note carries an interest rate of twelve percent on outstanding draws and matures on June 30, 2017. At any time prior to, or on the maturity date, Tabatabai Investment Partners LP has the option to convert all or any portion of the principal balance and accrued but unpaid interest then outstanding under the Note into shares of the Company's Common Stock, calculated by dividing the amount being converted by \$3.50. As of the maturity date, the Note permits the repayment of draws and interest to be in the Company's Common Stock at market prices, calculating the number of shares of the Company's Common Stock to be issued by dividing the amount being converted by \$3.50. The Note includes customary default, change control and acceleration provisions. The Company made a draw under this agreement in August 2016 for \$750,000.

The Company entered into a Stock Purchase Agreement ("SPA") with Tabatabai Investment Partners LP, to issue Company Common Stock in exchange for receiving \$250,000 on April 8, 2016. It was also agreed that Tabatabai would cancel \$300,000 of indebtedness in exchange for a number of shares of Common Stock of DATATRAK equal to the amount of \$300,000 divided by the price per share equal to \$3.50. Common Shares totaling 157,142 were issued to Tabatabai Investment Partners LP based on a market price of \$3.50 under this agreement as of April 5, 2016.

Furthermore, DATATRAK continuously evaluates its cost structure to timely match its cost structure with anticipated revenue and backlog. Although the Company has recently made strategic investments in its infrastructure in order to support longer-term growth,

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DATATRAK will continue to carefully evaluate its cost structure and implement cost cutting measures if its revenue and sales trend performance falls below its minimum expectations. In such an event, DATATRAK may also require additional short-term funding. The Company may need to raise additional funds to offset delays or cancellations of existing contracts, insufficient generation of new contracts, or to cover liquidity needs beyond 2016. DATATRAK may raise additional funds by selling debt or equity securities, by entering into strategic relationships or through other arrangements. Additional capital may not be available on acceptable terms, if at all. To the extent that additional equity capital is raised, it could have a dilutive effect on the existing shareholders.

Inflation

To date, the Company believes the effects of inflation have not had a material adverse effect on its results of operations or financial condition.

Information about Forward-Looking Statements

Certain statements made in this quarterly report, written materials or orally by the Company or its representatives may constitute forward-looking statements that are based on management's current beliefs, estimates and assumptions concerning the operations, future results and prospects of the Company and the clinical pharmaceutical research industry in general. All statements that address operating performance, events or developments that management anticipates will occur in the future, including statements related to future revenue, profits, expenses, cost reductions, cash management alternatives and working capital requirements, exploration of strategic alternatives, raising additional funds, income and earnings per share or statements expressing general optimism about future results, are forward-looking statements. In addition, words such as "expects," "anticipates," "intends," "plans," "believes," "estimates," variations of such words, and similar expressions are intended to identify forward-looking statements. Factors that may cause actual results to differ materially from those in the forward-looking statements include the limited operating history on which the Company's performance can be evaluated; the ability of the Company to continue to enhance its software products to meet customer and market needs; fluctuations in the Company's quarterly results; the viability of the Company's business strategy and its stage of development; the timing of clinical trial sponsor decisions to conduct new clinical trials or cancel or delay ongoing trials; the Company's dependence on major customers; government regulation associated with clinical trials and the approval of new drugs; the ability of the Company to compete in the evolving EDC market; losses that potentially could be incurred from breaches of contracts or loss of customer data; the inability to protect intellectual property rights or the infringement upon other's intellectual property rights; the outcome of the Company's litigation; the costs associated with maintaining and/or developing the *DATATRAK ONE[®] Unified Experience[™]* software suite; uncertain impact on customers and contracts as a result of the recent or future economic downturns; and general economic conditions such as the rate of employment, inflation, interest rates and the condition of capital markets. This list of factors is not all inclusive. In addition, the Company's success depends on the outcome of various strategic initiatives it has undertaken, all of which are based on assumptions made by the Company concerning trends in the clinical research market and the health care industry. Any forward-looking statement speaks only as of the date on which such statement is made and the Company does not undertake any obligation to update any statements whether as a result of new information, future events or otherwise.

B. Date and State (or Jurisdiction) of Incorporation:

Ohio, July 17, 1991

C. The issuer's primary and secondary SIC Codes;

The primary and secondary SIC codes are 7374 and 7372, respectively.

D. The issuer's fiscal year end date;

December 31st

E. Principal products or services, and their markets;

The Company's products were originally developed to provide data to sponsors of clinical research trials faster and more efficiently than other competing systems, including paper-based solutions. Automating data entry and review procedures under a single architecture can save time in the drug development and medical device approval process, and possibly result in enhanced patient safety. The DATATRAK system consists of numerous modules designed for custom configurability to each clinical research process. The Company initially provides a set of electronic case report forms specific to the protocol of each clinical trial. Each

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patient's casebook is available for data entry by the respective research site participating in the clinical trial via a secure connection over the Internet. Once clinical trial data has been collected and entered, the clinical trial sponsor, or other contracted vendor, can review the data remotely from any internet connected device. As the data is reviewed and cleansed of all entry errors, the system generates standard and ad-hoc reports to facilitate the data cleaning process and to monitor patient safety. Finally, the software's export feature allows completed data and reports to be transmitted directly to a clinical trial sponsor's in-house database or for FDA submission – all in real-time.

The *DATATRAK ONE® Unified Experience™* software suite provides the following capabilities: CTMS; EDC, including medical coding; digitized electrocardiograms; image collection, viewing and storing capabilities; interactive response technologies, including randomization and clinical supply management; safety case management; clinical trial design, including mid-study changes; clinical file repository for data and study assets; content-based training supported by a learning management system (“LMS”), and workgroup collaboration capabilities. Additional enhancements in late 2014 provided analysis and reporting functionality across solutions, specifically *UX EDC™* and *UX RTSM™* through the Cross-Study toolset. Extensive work was completed in 2016 on the next generation CTMS solution, *UX CTMS 360™*, which again leverages cross solution functionality in reporting and analysis. The Company believes the new solution will transform how the industry measures return on investment (“ROI”) on software purchases, opening the door for continued increase in multi-solution purchases by current and potential clients.

DATATRAK built its multi-component, comprehensive solution through a single, unified clinical research platform leveraging a single database architecture and expanded this concept to include services delivery from the *DATATRAK* Clinical and Consulting Services (“DCCS”) group. The Company delivers a complete portfolio of software products designed to accelerate the reporting of clinical research data from sites to sponsors and ultimately regulatory authorities more efficiently than loosely integrated technologies. The *DATATRAK ONE®* unified software solution, deployed worldwide through its cloud offering, supports pre-clinical and Phase I – Phase IV drug and device studies in multiple languages throughout the world.

DATATRAK Clinical and Consulting Services, or DCCS, offers support to our clients in the Preclinical and Phase I – Phase IV trials. Starting with the final protocol, DCCS can conduct most clinical data management services from study start-up through study close-out. In 2015, *DATATRAK* discontinued Clinical Data Manager (“CDM”) services that were seen as competitive with our client base. The *DATATRAK* Project Management team tracks study deliverables, including interim data transfers if required by the client, or data cuts, data locks and ad-hoc requests. As the study comes to a close, DCCS assists in the finalization or ‘locking’ of the database and performs the study data archival. In addition to clinical trial specific services, DCCS also offers clinical and technology consulting as well as rescue study and migration expertise.

DATATRAK has partner and enterprise transfer programs to empower customers to design, deploy and manage their clinical trials independently through the Company's cloud-based delivery. *DATATRAK* has found that customers desire to be as independent as possible in the performance of their clinical trials. This trend is another growth aspect of the industry that is believed to be gaining momentum.

7) Describe the Issuer's Facilities

As of September 30, 2016, the Company was leasing approximately 4,300 square feet of office space in Mayfield Heights, Ohio. This space is used for its headquarters and U.S. operations. In addition, *DATATRAK* has U.S. based operations in Bryan, Texas, where the Company leases approximately 2,300 square feet of office space. The Company had leased approximately 6,400 square feet of office space in Cary, North Carolina. *DATATRAK* entered into an assignment agreement for the office space in Cary, North Carolina, which was effective as of April 5, 2016 and no longer bears any financial liability for the lease. The Company entered into a sublease agreement as of July 7, 2016 for the 14,000 square feet of office space in Chicago, Illinois in order to mitigate the expense associated with the original lease. For additional information regarding the master lease for the Chicago office space, see Note 7. Operating Leases to the condensed consolidated financial statements included in this report.

8) Officers, Directors, and Control Persons

A. The names of Officers and Directors as of September 30, 2016 are as follows:

<u>Name</u>	<u>Position</u>
Alex Tabatabai	Chairman of the Board of Directors Chairman of the Audit Committee

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Jack H. Jacobs	Director Chairman of the Compensation Committee Chairman of the Nominating & Governance Committee
Dr. Eric J. Wilhelm	Director
James R. Ward	Chief Executive Officer and President
	Director
Julia Henderson	Chief Financial Officer and Treasurer

The following persons are control persons as they beneficially owned 5% or more of *DATATRAK* stock as of September 30, 2016:

Tabatabai Investment Management LLC (f/k/a Arosa Investment Management LLC) ^{1 2}	540 N. Dearborn St. #101257 Chicago, IL 60610	351,165 Common Shares
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¹Tabatabai Investment Management LLC is controlled by Alex Tabatabai, Chairman of the Board of Directors of the Company.

² All Common Shares are held by Tabatabai Investment Management LLC (formerly known as Arosa Investment Management LLC), which is controlled by Mr. Tabatabai, Chairman of the Board of Directors of the Company. Dr. Wilhelm, Dr. Mirza and Mr. Ben Tabatabai are limited partners in Tabatabai Investment Partners LP, whose general partner is Tabatabai Investment Management LLC. The number of Common Shares listed in the table above does not include any shares that may be received by Tabatabai Investment Partners LP upon conversion of the convertible promissory notes. There was \$750,000 drawn by the Company under this convertible note agreement as of September 30, 2016. If the draw was converted as of September 30, 2016, approximately 218,000 additional shares would be issued.

The disclosure is limited to those whose holdings the Company knows or can verify.

B. Legal/Disciplinary History.

1. A conviction in a criminal proceeding or named as a defendant in a pending criminal proceeding (excluding traffic violations and other minor offenses);

None

2. The entry of an order, judgment, or decree, not subsequently reversed, suspended or vacated, by a court of competent jurisdiction that permanently or temporarily enjoined, barred, suspended or otherwise limited such person's involvement in any type of business, securities, commodities, or banking activities;

None

3. A finding or judgment by a court of competent jurisdiction (in a civil action), the Securities and Exchange Commission, the Commodity Futures Trading Commission, or a state securities regulator of a violation of federal or state securities or commodities law, which finding or judgment has not been reversed, suspended, or vacated; or

None

4. The entry of an order by a self-regulatory organization that permanently or temporarily barred suspended or otherwise limited such person's involvement in any type of business or securities activities.

None

C. Beneficial Shareholders. The following persons beneficially own more than 10% of *DATATRAK* Common Stock as of September 30, 2016:

Tabatabai Investment Management LLC (f/k/a Arosa)	540 N. Dearborn St. #101257 Chicago, IL 60610	351,165 Common Shares
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Investment Management LLC) ^{1 2}		
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¹Tabatabai Investment Management LLC is controlled by Alex Tabatabai, Chairman of the Board of Directors of the Company.

² All Common Shares are held by Tabatabai Investment Management LLC (formerly known as Arosa Investment Management LLC), which is controlled by Mr. Tabatabai, Chairman of the Board of Directors of the Company. Dr. Wilhelm, Dr. Mirza and Mr. Ben Tabatabai are limited partners in Tabatabai Investment Partners LP, whose general partner is Tabatabai Investment Management LLC. The number of Common Shares listed in the table above does not include any shares that may be received by Tabatabai Investment Partners LP upon conversion of the convertible promissory notes. There was \$750,000 drawn by the Company under this convertible note agreement as of September 30, 2016. If the draw was converted as of September 30, 2016, approximately 218,000 additional shares would be issued.

The disclosure is limited to those whose holdings the Company knows or can verify.

9) Third Party Providers

Please provide the name, address, telephone number, and email address of each of the following outside providers that advise your company on matters relating to operations, business development and disclosure:

Legal Counsel

Thompson Hine LLP
3900 Key Center, 127 Public Square
Cleveland, OH 44114
Phone: (216) 566-5500
Derek.Bork@ThompsonHine.com

Calfee Halter & Griswold LLP
The Calfee Building
1405 East Sixth St.
Cleveland, OH 44114
Phone: (216) 622-8200
info@calfee.com

Ogletree Deakins
127 Public Square #4100
Cleveland, OH 44114
Phone: (216) 241-6100
Bruce.Hearey@Ogletreedeakins.com

Auditor

Skoda Minotti & Co.
6685 Beta Drive.
Mayfield Village, OH 44143
Phone: (440) 449-6800
RSiebel@skodaminotti.com

Other Advisor:

DiCillo & Associates
7500 Town Centre Dr.
Suite 500
Broadview Heights, OH 44147
Phone: (216) 377-1950
ddicillo@greatlakescpa.net

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10) Issuer Certification

I, James R. Ward, Chief Executive Officer and President of *DATATRAK International, Inc.*, certify that:

1. I have reviewed this quarterly disclosure statement of *DATATRAK International, Inc.*;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

Date: November 1, 2016

/s/ James R. Ward

James R. Ward

Chief Executive Officer and President

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10) Issuer Certification (continued)

I, Julia Henderson, Chief Financial Officer of *DATATRAK* International, Inc., certify that:

1. I have reviewed this quarterly disclosure statement of *DATATRAK* International, Inc.;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

Date: November 1, 2016

/s/ Julia Henderson

Julia Henderson

Chief Financial Officer, Treasurer (Principal Financial Officer)

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EXHIBIT 10.39

EMPLOYMENT AGREEMENT

This EMPLOYMENT AGREEMENT (this “Agreement”) is made and entered into as of May ____, 2016, by and between Datatrak International, Inc., an Ohio corporation (the “Company”), and Julia Henderson, an individual resident of the State of Ohio (the “Executive”).

WHEREAS, the parties desire to enter into this Agreement pertaining to the employment of the Executive by the Company.

NOW, THEREFORE, in consideration of the mutual covenants and agreements set forth below, it is hereby covenanted and agreed by the Company and the Executive as follows:

1. Employment. The Company hereby agrees to employ the Executive and the Executive hereby agrees to be employed by the Company upon the terms and conditions hereinafter set forth.

2. Duties and Services.

(a) Title and Duties. The Executive shall serve as the Chief Financial Officer of the Company, with the authority, responsibilities and duties customarily exercised by a person holding that position in a company that has stock listed for trading on the OTC Markets, with such additions or modifications thereto that are consistent with her authority, responsibilities and duties hereunder as the Board of Directors of the Company may from time to time in its discretion adopt.

(b) Time. The Executive shall devote her full business time and attention to the business and affairs of the Company and to the promotion of the Company’s best interests, which shall include the devotion of a minimum of forty (40) hours per week, subject to authorized paid time off and holidays. Notwithstanding the foregoing, the Executive may acquire passive investment interests in one or more entities that do not compete with the Company or any of its subsidiaries; provided that such activities do not inhibit or interfere with the performance of the Executive’s duties under this Agreement. The Executive shall at all times comply with all Company policies that are adopted by the Board of Directors from time to time.

(c) Travel. The Executive shall undertake such travel as may be necessary and desirable to promote the business and affairs of the Company, consistent with the Executive’s position and duties with the Company.

3. Term of Employment. The term of this Agreement shall be a period of one (1) year; provided that the Executive’s employment shall be on an at-will basis, meaning that either the Company or the Executive may terminate the Executive’s employment at any time and for any reason, with or without cause.

4. Compensation.

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(a) Base Salary. For all of the services to be rendered by the Executive under this Agreement, the Company shall pay the Executive a base salary at a rate equal to \$140,000 in cash per year (the “Base Salary”). The Base Salary shall be paid to the Executive in accordance with the normal payroll practices of the Company and shall be subject to customary withholding taxes and other employment taxes as required by applicable law.

(b) Employee Benefits. The Executive shall be entitled to participate in any employee benefits plans or programs that may generally be maintained from time to time by the Company for its employees, to the extent permitted by applicable law.

(c) Vacation. The Executive shall be entitled to vacation each calendar year in accordance with the applicable Company policy. During all vacation time, the Executive’s Base Salary and other benefits as stated herein shall continue to be provided in full. Such vacation time shall be taken at times convenient for the Company and upon advance notice to the Board of Directors of the Company.

(d) Cash Bonus. The Executive will be eligible to receive a cash bonus in an amount equal to \$40,000 (the “Cash Bonus”) in the event that the Company achieves positive net income (after application of the Cash Bonus) for the fiscal year ended December 31, 2016 as reported in the financial statements of the Company filed with the OTC Markets. If payable, the Cash Bonus shall be paid to the Executive promptly after the Company files its annual report with the OTC Markets for the 2016 fiscal year and in accordance with the normal payroll practices of the Company and shall be subject to customary withholding taxes and other employment taxes as required by applicable law.

(e) Equity Bonus. The Executive will be eligible to receive an equity bonus award of 10,000 shares of restricted Common Stock of the Company (the “Equity Bonus”) in the event that the Company achieves at least \$1,000,000 in net income (after application of the Cash Bonus) for the fiscal year ended December 31, 2016 as reported in the financial statements of the Company filed with the OTC Markets. If payable, the Equity Bonus shall be granted to the Executive promptly after the Company files its annual report with the OTC Markets for the 2016 fiscal year and pursuant to the Company’s applicable equity incentive plan and standard form of award agreement.

5. Expense Reimbursement. The Executive shall be entitled to prompt reimbursement for all pre-approved expenses incurred by her in the performance of her duties hereunder, upon submission and approval of written statements and receipts in accordance with the then-applicable policies of the Company.

6. Confidentiality and Invention Assignment Agreement. On the date of this Agreement, the Executive shall enter into the form of Confidentiality and Invention Assignment Agreement attached hereto as Exhibit A.

7. Representations and Warranties. The Executive represents and warrants to the Company that she is subject to no contractual or other restriction or obligations which are inconsistent with the execution of this Agreement, or which may interfere with the performance of her duties hereunder. The Executive represents and warrants that the execution and performance of this Agreement by her will not violate any policies or procedures of any other person or entity for which she performs or has performed any services or been employed.

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8. Indemnification. The Company shall indemnify the Executive to the fullest extent permitted by the applicable laws of the State of Ohio, in effect at the time of the subject act or omission, and shall advance to the Executive reasonable attorney's fees and expenses as such fees and expenses are incurred (subject to an undertaking from the Executive to repay such advances if it shall be determined by a court of competent jurisdiction that the Executive was not entitled to reimbursement of such fees and expenses), in each case against all costs, charges and expenses incurred or sustained by the Executive in connection with any action, suit or proceeding to which the Executive may be made a party by reason of her being or having been a director, officer or employee of the Company or any subsidiary of the Company (other than any dispute, claim or controversy arising under or relating to this Agreement). The Executive shall be entitled to the protection of any directors and officers liability insurance policies that the Company may elect to maintain generally for the benefit of its directors and officers during the term of her employment with the Company.

9. Termination of Employment. Upon the termination of the Executive's employment for any reason, the Executive or, in the event of her death, the Executive's estate shall be entitled to the Executive's Base Salary prorated through the date of termination. Any employee benefits to which the Executive is entitled by reason of her employment shall be paid to the Executive or her estate, as applicable, at such time as is provided by the terms of the applicable Company plan or policy.

10. Officer Resignation. Upon termination of her employment with the Company for any reason, the Executive shall be deemed to have resigned, as of the date of such termination, from any and all offices held with the Company or any of its subsidiaries.

11. Modifications and Waivers. No provision of this Agreement may be modified, waived or discharged unless that modification, waiver or discharge is agreed to in writing by the Executive and the Company. No waiver by either party at any time of any breach by the other party of, or compliance with, any condition or provision of this Agreement to be performed by the other party shall be deemed a waiver of any other provisions or conditions at the time, or at any prior or subsequent time.

12. Governing Law. The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of Ohio, notwithstanding any conflict of law provision to the contrary.

13. Successors and Assigns. This Agreement shall be binding upon, and shall inure to the benefit of, the parties hereto and their respective heirs, beneficiaries, personal representatives, successors and assigns.

14. Notices. Any notice, request or other communication required to be given pursuant to the provisions of this Agreement shall be in writing and shall be deemed to have been given when delivered in person, on the next business day after being delivered to a nationally-recognized overnight courier service (for next-day delivery) or five (5) days after being deposited in the United States mail, certified or registered, postage prepaid, return receipt requested and addressed, in the case of the Company, to the principal executive offices of the Company and, in the case of the Executive, to the address of the Executive on file with the Company.

15. Entire Agreement. This Agreement constitutes the entire agreement between the parties concerning the subject matter hereof and supersedes all prior and contemporaneous agreements, if any, between the parties relating to the subject matter hereof.

DATATRAK International, Inc.

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16. Counterparts. This Agreement may be executed in counterparts, each of which shall take effect as an original and each of which shall evidence one and the same agreement.

[signatures follow on the next page]

DATATRAK International, Inc.

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IN WITNESS WHEREOF, the parties hereto have executed this Agreement on the date and year first above written.

DATATRAK INTERNATIONAL, INC.

JULIA HENDERSON

By: /s/ Alex Tabatabai

/s/ Julia Henderson

Name: Alex Tabatabai

Title: Chairman of the Board of Directors

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EXHIBIT 10.40

EMPLOYMENT AGREEMENT

This EMPLOYMENT AGREEMENT (this “Agreement”) is made and entered into as of October 1, 2016, by and between Datatrak International, Inc., an Ohio corporation (the “Company”), and James R. (“Jim Bob”) Ward, an individual resident of the State of Ohio (the “Executive”).

WHEREAS, the parties desire to enter into this Agreement pertaining to the employment of the Executive by the Company.

NOW, THEREFORE, in consideration of the mutual covenants and agreements set forth below, it is hereby covenanted and agreed by the Company and the Executive as follows:

1. Employment. The Company hereby agrees to employ the Executive and the Executive hereby agrees to be employed by the Company upon the terms and conditions hereinafter set forth.

2. Duties and Services.

(a) Title and Duties. The Executive shall serve as the President and Chief Executive Officer of the Company, with the authority, responsibilities and duties customarily exercised by a person holding such positions in a company that has stock listed for trading on the OTC Markets, with such additions or modifications thereto that are consistent with the Executive’s authority, responsibilities and duties hereunder as the Board of Directors of the Company may from time to time in its discretion adopt.

(b) Time. The Executive shall devote the Executive’s full business time and attention to the business and affairs of the Company and to the promotion of the Company’s best interests, which shall include the devotion of a minimum of forty (40) hours per week, subject to authorized paid time off and holidays. Notwithstanding the foregoing, the Executive may acquire passive investment interests in one or more entities that do not compete with the Company or any of its subsidiaries; provided that such activities do not inhibit or interfere with the performance of the Executive’s duties under this Agreement. The Executive shall at all times comply with all Company policies that are adopted by the Board of Directors from time to time.

(c) Travel. The Executive shall undertake such travel as may be necessary and desirable to promote the business and affairs of the Company, consistent with the Executive’s position and duties with the Company.

3. Term of Employment. The term of this Agreement shall be a period of one (1) year; provided that the Executive’s employment shall be on an at-will basis, meaning that either the Company or the Executive may terminate the Executive’s employment at any time and for any reason, with or without cause.

4. Compensation.

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(a) Base Salary. For all of the services to be rendered by the Executive under this Agreement, the Company shall pay the Executive a base salary at a rate equal to \$220,000 in cash per year (the "Base Salary"). The Base Salary shall be paid to the Executive in accordance with the normal payroll practices of the Company and shall be subject to customary withholding taxes and other employment taxes as required by applicable law.

(b) Employee Benefits. The Executive shall be entitled to participate in any employee benefits plans or programs that may generally be maintained from time to time by the Company for its employees, to the extent permitted by applicable law.

(c) Vacation. The Executive shall be entitled to vacation each calendar year in accordance with the applicable Company policy. During all vacation time, the Executive's Base Salary and other benefits as stated herein shall continue to be provided in full. Such vacation time shall be taken at times convenient for the Company and upon advance notice to the Board of Directors of the Company.

(d) Cash Bonus. The Executive will be eligible to receive an annual incentive cash bonus (the "Cash Bonus") in an amount, and subject to such performance conditions and/or metrics, as shall be determined prior to each fiscal year by the Compensation Committee of the Board of Directors of the Company. If payable, the Cash Bonus shall be paid to the Executive promptly after the Company files its annual report with the OTC Markets for the applicable fiscal year and in accordance with the normal payroll practices of the Company and shall be subject to customary withholding taxes and other employment taxes as required by applicable law.

(e) Equity Awards. The Executive will be eligible to receive equity compensation awards at such time and upon such terms and conditions as shall be determined from time to time by the Compensation Committee of the Board of Directors of the Company.

(f) Immediate Equity Grant. In consideration of the Executive's service as President and Chief Executive Officer of the Company since February 23, 2016 for \$1.00 per month, on the date hereof the Company shall grant to the Executive 20,000 shares of common stock of the Company. The Executive understands that the common stock issued hereunder shall be "restricted stock" within the meaning of the Securities Act of 1933 and the rules and regulations thereunder.

5. Expense Reimbursement. The Executive shall be entitled to prompt reimbursement for all pre-approved expenses incurred by the Executive in the performance of the Executive's duties hereunder, upon submission and approval of written statements and receipts in accordance with the then-applicable policies of the Company.

6. Confidentiality and Invention Assignment Agreement. On the date of this Agreement, the Executive shall enter into the form of Confidentiality and Invention Assignment Agreement attached hereto as Exhibit A.

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7. Representations and Warranties. The Executive represents and warrants to the Company that the Executive is subject to no contractual or other restriction or obligations which are inconsistent with the execution of this Agreement, or which may interfere with the performance of the Executive's duties hereunder. The Executive represents and warrants that the execution and performance of this Agreement by the Executive will not violate any policies or procedures of any other person or entity for which the Executive performs or has performed any services or been employed.

8. Indemnification. The Company shall indemnify the Executive to the fullest extent permitted by the applicable laws of the State of Ohio, in effect at the time of the subject act or omission, and shall advance to the Executive reasonable attorney's fees and expenses as such fees and expenses are incurred (subject to an undertaking from the Executive to repay such advances if it shall be determined by a court of competent jurisdiction that the Executive was not entitled to reimbursement of such fees and expenses), in each case against all costs, charges and expenses incurred or sustained by the Executive in connection with any action, suit or proceeding to which the Executive may be made a party by reason of the Executive being or having been a director, officer or employee of the Company or any subsidiary of the Company (other than any dispute, claim or controversy arising under or relating to this Agreement). The Executive shall be entitled to the protection of any directors and officers liability insurance policies that the Company may elect to maintain generally for the benefit of its directors and officers during the term of the Executive's employment with the Company.

9. Termination of Employment. Upon the termination of the Executive's employment for any reason, the Executive or, in the event of the Executive's death, the Executive's estate shall be entitled to the Executive's Base Salary prorated through the date of termination. Any employee benefits to which the Executive is entitled by reason of the Executive's employment shall be paid to the Executive or the Executive's estate, as applicable, at such time as is provided by the terms of the applicable Company plan or policy.

10. Officer Resignation. Upon termination of the Executive's employment with the Company for any reason, the Executive shall be deemed to have resigned, as of the date of such termination, from any and all offices held with the Company or any of its subsidiaries.

11. Modifications and Waivers. No provision of this Agreement may be modified, waived or discharged unless that modification, waiver or discharge is agreed to in writing by the Executive and the Company. No waiver by either party at any time of any breach by the other party of, or compliance with, any condition or provision of this Agreement to be performed by the other party shall be deemed a waiver of any other provisions or conditions at the time, or at any prior or subsequent time.

12. Governing Law. The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of Ohio, notwithstanding any conflict of law provision to the contrary.

13. Successors and Assigns. This Agreement shall be binding upon, and shall inure to the benefit of, the parties hereto and their respective heirs, beneficiaries, personal representatives, successors and assigns.

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14. Notices. Any notice, request or other communication required to be given pursuant to the provisions of this Agreement shall be in writing and shall be deemed to have been given when delivered in person, on the next business day after being delivered to a nationally-recognized overnight courier service (for next-day delivery) or five (5) days after being deposited in the United States mail, certified or registered, postage prepaid, return receipt requested and addressed, in the case of the Company, to the principal executive offices of the Company and, in the case of the Executive, to the address of the Executive on file with the Company.

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16. Counterparts. This Agreement may be executed in counterparts, each of which shall take effect as an original and each of which shall evidence one and the same agreement.

[signatures follow on the next page]

DATATRAK International, Inc.

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IN WITNESS WHEREOF, the parties hereto have executed this Agreement on the date and year first above written.

DATATRAK INTERNATIONAL, INC.

JAMES R. WARD

By: /s/ Alex Tabatabai

/s/ James R. Ward

Name: Alex Tabatabai

Title: Chairman of the Board of Directors