

**ALLIANCE MEDIA HOLDINGS INC.
AND SUBSIDIARIES**

Consolidated Financial Statements

June 30, 2020

ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
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ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED BALANCE SHEET

JUNE 30, 2020

(In thousands, except per share amounts)

ASSETS

CURRENT ASSETS:

Cash and equivalents	\$424
Accounts receivable-net	131
Prepaid expenses and other current assets	<u>13</u>

Total current assets 568

PROPERTY AND EQUIPMENT - NET 12

OTHER ASSETS 3

TOTAL \$583

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

Bank loan payable	\$ 259
Accounts payable	77
Accrued expenses and other current liabilities	568
Deferred revenues	88
Accounts payable associated with discontinued operations	<u>367</u>

Total current liabilities 1,359

COMMITMENTS AND CONTINGENCIES

NON-CONTROLLING INTEREST (115)

STOCKHOLDERS' EQUITY:

Series A Convertible Non-Redeemable Preferred Stock, \$.001 par value; 8,269 shares authorized; no shares issued and outstanding	-
Common stock, \$.001 par value; 100,000 shares authorized; 44,184 shares issued and outstanding	44
Additional paid-in capital	4,295
Accumulated deficit	<u>(5,000)</u>
Total deficit	<u>(661)</u>

TOTAL \$ 583

See notes to unaudited consolidated financial statements.

ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENT OF OPERATIONS
YEAR ENDED JUNE 30, 2020
(In thousands, except per share amounts)

Net revenues	<u>\$1,987</u>
Cost of sales	89
Operating costs and expenses	<u>2,457</u>
	<u>2,546</u>
Consolidated loss from continuing operations	(559)
Loss attributable to noncontrolling interest	<u>83</u>
Loss from continuing operations attributable to Alliance Media Holdings Inc.	(476)
Loss from discontinued operations	<u>126</u>
Net loss attributable to Alliance Media Holdings Inc.	<u>\$ (602)</u>
Net loss per share attributable to Alliance Media Holdings Inc. Basic and diluted	<u>\$(0.01)</u>
Weighted-average common shares outstanding – basic and diluted	<u>44,184</u>

See notes to unaudited consolidated financial statements.

ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT
YEAR ENDED JUNE 30, 2020
(In thousands)

	Preferred Stock		Common Stock		Additional	Accumulated	Total
	Shares	Amount	Shares	Amount	Paid-in Capital	Deficit	Stockholders' Deficit
Balance, July 1, 2019	-	\$ -	44,184	\$44	\$4,252	\$(4,398)	\$ (102)
Stock-based compensation expense	-	-	-	-	43	-	43
Net loss attributable to Alliance Media Holdings Inc.	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(602)</u>	<u>(602)</u>
Balance, June 30, 2020	<u>-</u>	<u>\$ -</u>	<u>44,184</u>	<u>\$44</u>	<u>\$4,295</u>	<u>\$(5,000)</u>	<u>\$(661)</u>

See notes to unaudited consolidated financial statements.

ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2020
(In thousands)

OPERATING ACTIVITIES:

Net loss - consolidated	\$(685)
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation and amortization	9
Stock-based compensation expense	43
Other	2
Changes in operating assets and liabilities:	
Accounts receivable	115
Inventory	200
Prepaid expenses and other assets	69
Accounts payable	(38)
Accrued expenses and other current liabilities	332
Deferred revenues	<u>50</u>
Net cash provided by operating activities	<u>97</u>

INVESTING ACTIVITIES:

Purchase of property and equipment	<u>(6)</u>
Net cash used in investing activities	<u>(6)</u>

FINANCING ACTIVITIES:

Payment of asset-based revolving loan - bank, net of proceeds	(135)
Proceeds from bank loan	<u>259</u>
Net cash provided by financing activities	<u>124</u>

NET INCREASE IN CASH AND EQUIVALENTS 215

CASH AND EQUIVALENTS, BEGINNING OF YEAR 209

CASH AND EQUIVALENTS, END OF YEAR \$ 424

See notes to unaudited consolidated financial statements.

ALLIANCE MEDIA HOLDINGS INC. AND SUBSIDIARIES
Notes to Unaudited Consolidated Financial Statements

Note 1 - THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Alliance Media Holdings Inc. is a developer and publisher of console and downloadable video games. We own two development studios: Zachtronics and Starcolt Studios, both of which develop and publish console and downloadable video games. We also publish third party licensed video games as Alliance Digital Media and as Alliance Games. The consolidated financial statements include the accounts of Alliance Media Holdings Inc. and its wholly-owned subsidiaries, as well as its New Zealand based majority-owned company Starcolt Studios Limited. The non-controlling interests in Starcolt Studios Limited are accounted for in accordance with Financial Accounting Standards Board (FASB) non-controlling interest guidance. All significant intercompany accounts and transactions have been eliminated in consolidation.

As a result of the industry shift from the sale of physical boxed video games to downloadable digital content, we discontinued our distribution operations and liquidated our physical inventory.

Going Concern

We have prepared our consolidated financial statements using the generally accepted accounting principles applicable to a going concern, which contemplate the realization of assets and liquidation of liabilities in the normal course of business. Principally as a result of the industry's economic environment which resulted in the discontinuation of our distribution business, we have reported a substantial operating loss for the fiscal year ended June 30, 2020. Furthermore, as described in Note 6 to the consolidated financial statements, we have to date been unable to replace our revolving bank loan which expired on September 30, 2019. As a result, substantial doubt exists about our ability to continue as a going concern.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates reflected in these financial statements relate primarily to the amortization of deferred revenues, the realization of deferred tax assets and valuation of stock-based compensation.

Cash and Equivalents

For financial statement purposes (including cash flows), we consider all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents.

Property and Equipment

Property and equipment is recorded at cost. Expenditures for major additions and improvements are capitalized and minor replacements, maintenance and repairs are charged to expense as incurred. Leasehold improvements are amortized over the lesser of the lease terms or the assets' useful lives. When property and equipment is retired or otherwise disposed of, the cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is included in the results of operations for the respective period. Depreciation and amortization is provided over the estimated useful lives of the related assets using the straight-line method.

The estimated useful lives for significant property and equipment categories are as follows:

Leasehold improvements	up to 4 years
Computers, office equipment and furniture	2 to 7 years
Computer software	2 to 3 years

Software Development Costs

Capitalized software development costs include direct costs incurred for internally-developed titles and, when applicable, payments made to third-party software developers under development agreements (see Note 4).

Internal software development costs, third-party production and other content costs are capitalized subsequent to establishing technological feasibility of a software title. Technological feasibility of a product encompasses both technical design documentation and game design documentation, or the completed and tested product design and working model. Significant management judgments and estimates are utilized in the assessment of when technological feasibility is established. For products where proven technology exists, this may occur early in the development cycle. Technological feasibility is evaluated on a product-by-product basis.

From time to time, we enter into agreements with third-party independent developers that require it to make payments for game development and production services. In exchange for such payments, we receives publishing and distribution rights to the finished game title as well as, in some cases, a portion of the underlying intellectual property rights. Such agreements typically allow for the recovery of these payments to the developers at an agreed-upon royalty rate earned on the subsequent sales of such software, net of any agreed-upon costs. Prior to establishing technological feasibility of a product, costs incurred by third-party developers are reflected as research and development expenses. Subsequent to establishing technological feasibility of a product, development and production service payments to third-party developers are capitalized as software development costs and licenses.

Amortization of capitalized software development costs and licenses commences when a product is released and is recorded on a title-by-title basis in cost of goods sold. For capitalized software development costs, amortization is calculated using (1) the proportion of current year revenues to the total revenues expected to be recorded over the life of the title or (2) the straight-line method over the remaining estimated useful life of the title, whichever is greater. For capitalized licenses, amortization is calculated as a ratio of (1) current period revenues to the total revenues expected to be recorded over the remaining life of the title or (2) the contractual royalty rate based on actual net product sales as defined in the licensing agreement, whichever is greater.

We evaluate the remaining future recoverability of capitalized software development costs and licenses on a quarterly basis. Recoverability is primarily assessed based on the actual title's performance. For products that are scheduled to be released in the future, recoverability is evaluated based on the expected performance of the specific products to which the cost or license relates, utilizing criteria including historical performance of similar products developed with comparable technology; market performance of similar titles and general market conditions. When it is determined that the value of the title is unlikely to be recovered by product sales, capitalized costs are charged to cost of sales in the period in which such determination is made.

Impairment of Long-Lived Assets

Long-lived assets, such as property, plant and equipment, and intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. We assess our assets for impairment based on the estimated future undiscounted cash flows expected to result from the use of the asset and records impairment losses when this amount is less than the carrying amount. Impairment losses are recorded for the excess of the assets' carrying amount over their fair value, which is generally determined based on the estimated future discounted cash flows over the remaining useful life of the asset using a discount rate determined by us at the date of the impairment review. We believe at this time that the carrying value and useful life of long-lived assets continue to be appropriate.

Revenue Recognition

We principally derive our revenues from the sale of its digitally delivered full-play video games sold through third party digital content distribution channels ("digital storefronts") and from the licensing of its games to third parties for inclusion in the third-party's hosted subscription-based offerings.

We recognize revenues in accordance with ASC Topic 606, Revenue From Contracts with Customers, pursuant to which we evaluate and recognizes revenues by (a) identifying our contract(s) and contractual performance obligations, (b) determining the transaction price, (c) allocating the transaction price to performance obligations in the contract and (d) recognizing revenue as each performance obligation is satisfied through the transfer of a promised good or service to a

customer (i.e., “transfer of control”).

Our products are sold as full games, which typically provide access to the main game content, primarily for console and PC. Generally, the full game software products deliver a license of our intellectual property that provides a functional offline gaming experience (i.e., one that does not require an Internet connection to access the main game content or other significant game related services). We recognize revenue related to the license of our intellectual property at the time control of the product has been digitally made available by the third-party digital storefront to the end user for download (i.e. upon delivery of the software product). Revenue is recorded net of both third-party digital storefront fees and of transaction taxes assessed by governmental authorities such as sales, value-added and other similar taxes.

We recognize revenue from the licensing of our games to third-party licensees for inclusion in the third-party’s hosted subscription-based offerings ratably over the term of the license.

In accordance with the criteria set forth in ASC 985-605, *Revenue Recognition*, we generally recognizes a sale of downloadable digital content when the download is purchased by a customer. Revenue for downloadable content sold via third party digital storefronts is recognized as revenue net of the fees retained by the storefront because we have determined that generally the third party is acting as the primary obligor in the sale to the end consumer.

Deferred Revenue

Deferred revenue is comprised primarily of contractual billings for licensing fees invoiced at the beginning of the contract period less the portion of such fees which have been ratably recognized as revenue. This balance increases from period to period by the amount of billed license fees being deferred and is reduced by the recognition of revenue from previously billed license fees.

Principal Agent Considerations

For sales of our software products via third party digital storefronts, we determine whether or not we are acting as the principal in the sale to the end user, which it considers in determining if revenue should be reported based on the gross transaction price to the end user or based on the transaction price net of fees retained by the third-party digital storefront. An entity is the principal if it controls a good or service before it is transferred to the customer. Key indicators used in evaluating these sales transactions include, but are not limited to, the underlying contract terms and conditions between the various parties to the transaction; which party is primarily responsible for fulfilling the promise to provide the specified good or service to the end customer; which party has inventory risk before the specified good or service has been transferred to the end customer; and which party has discretion in establishing the price for the specified good or service.

Based on an evaluation of the above indicators, we have determined that generally the third party is considered the principal to end customers for the sale of its product. As such, revenues related to these arrangements are reported net of the fees retained by the storefront.

Contract Balances

Accounts receivable related to revenue are generally recorded when we have an unconditional right to receive payment and deferred revenue is recorded when cash payments are received or due in advance of satisfying of revenue recognition. Allowance for doubtful accounts are typically immaterial and, if required, are based on our best estimate of probable losses inherent in the accounts receivable balance.

Accounts Receivable and Major Customers

Our revenue and accounts receivable are generated via certain platform providers, which subject us to a concentration of credit risk. One platform provider accounting for 52% of our revenues, a second platform provider accounted for 21% of our revenues and a third platform provider accounted for 10% of our revenues. In addition, 88% our accounts receivables at June 30, 2020 was from a single platform provided. Such receivable balance was subsequently collected in accordance with the contractual terms.

Income Taxes

We account for income taxes using the liability method, which requires the recognition of deferred tax assets or liabilities for the temporary differences between the financial reporting and tax bases of our assets and liabilities and for tax carryforwards at enacted statutory rates in effect for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. In addition, valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

We establish accruals for uncertain tax positions taken or expected to be taken in a tax return when it is more likely than not (i.e., a likelihood of more than fifty percent) that the position would be sustained upon examination by tax authorities that have full knowledge of all relevant information. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Favorable or unfavorable adjustment of the accrual for any particular issue would be recognized as an increase or decrease to income tax expense in the period of a change in facts and circumstances.

As of June 30, 2020, there are no unrecognized tax benefits, and there have been no income tax related interest or penalties accrued in the year ended June 30, 2020. If and when applicable, we will report interest expense and penalties related to income tax liabilities as a component of its provision for income taxes. Tax years commencing July 1, 2016 are subject to tax examination.

Advertising Costs

We generally expense promotion and advertising costs as incurred, except for production costs associated with media campaigns, which are recognized as prepaid assets (to the extent paid in advance) and expensed at the first run of the advertisement. Advertising costs for the year ended June 30, 2020 approximated \$13,000.

Research and Development

Research and development costs relate primarily to employee costs associated with game development and enhancement costs that do not meet the internal use software capitalization criteria. Such costs are expensed as incurred.

Contingent Acquisition Consideration

In connection with our 2016 acquisition of the video game assets of Zachtronics LLC in exchange for an annual earn out payment based upon a percentage of profits earned through June 2023 from video games completed prior to the acquisition date, during the current fiscal year ended June 30, 2020 an additional \$36,000 was accrued and is included as a component of cost of sales.

Fair Value of Financial Instruments

The carrying amounts of significant financial instruments, which include accounts receivable, accounts payable and accrued expenses, approximated fair value as of June 30, 2020 due to their short-term maturities. Borrowings under the financing agreements approximate fair value due to their variable interest rate.

Net Income (Loss) Per Share

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the period. Diluted net income (loss) per share is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding during the period increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued. The dilutive effect of the outstanding options is reflected in diluted earnings per share by application of the treasury stock method.

Stock-Based Compensation

We recognize compensation expense for all equity-based compensation awards issued to employees based on the grant date fair value of those awards.

Note 2 - SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

Supplemental disclosures of cash flow information are insignificant for the year ended June 30, 2020

Note 3 – DISCONTINUED OPERATIONS

As a result of the industry shift from the sale of physical boxed video games to downloadable digital content, during the current fiscal year ended June 30, 2020, we discontinued our distribution operations and liquidated our remaining physical inventory. The loss from discontinued operations presented in the consolidated statement of operations consists of the following:

Revenues	\$ 257,000
Cost of sales	(226,000)
Operating costs and expenses	(150,000)
Interest expense	<u>(7,000)</u>
Loss from discontinued operations	<u><u>\$(126,000)</u></u>

Accounts payable attributable to discontinued operations at June 30, 2020 was \$367,000.

Note 4 - SOFTWARE DEVELOPMENT COSTS

We did not capitalize software costs in the year ended June 30, 2020. Included in cost of sales is approximately \$63,000 of amortization expense from previously capitalized software development costs.

Note 5 - PROPERTY AND EQUIPMENT

Property and equipment stated at cost less accumulated depreciation and amortization (in thousands) principally consists of computers, office equipment and furniture. Depreciation and amortization expense approximated \$13,000.

Note 6 – BANK LOAN PAYABLE

In April 2020, we received loan we received loan proceeds of approximately \$259,000 under the Paycheck Protection Program (“PPP”) which was established as part of the Coronavirus Aid, Relief and Economic Security Act (“CARES Act”). The loans and accrued interest are forgivable, as long as the borrower uses the loan proceeds for eligible purposes, including payroll, benefits, rent and utilities, and maintains its payroll levels. The unforgiven portion of the loan, if any, is payable over two years at an interest rate of 1% per year, with a deferral of payments for the first six months.

We had a revolving, asset-based bank loan facility with PNC bank which had been in default and was repaid in full on September 30, 2019. Interest expense, which is a component of the loss from discontinued operations and includes the write-off of previously unamortized financing expenses, totaled approximately \$7,000.

Note 7 - INCOME TAXES

At June 30, 2020 we had federal net operating loss carryforwards (NOLs) of approximately \$8.2 million. In addition to the NOLs, we have other deferred tax assets aggregating approximately \$1.1. In assessing the realization of deferred tax assets, we consider whether it is more likely than not that all or some portion of the deferred tax assets will not be realized. The ultimate realization of the deferred tax assets is dependent upon the generation of future taxable income during the periods in which temporary differences are deductible and net operating losses are utilized. Based on a consideration of these factors, we have established a valuation allowance for the full amount of the deferred tax assets totaling approximately \$9.3 million primarily due to the uncertainty surrounding our ability to generate sufficient future taxable income to realize the deferred tax assets. We considered many factors when assessing the likelihood of future realization of the deferred tax assets, including our recent cumulative earnings experience, expectation of future income, and other relevant factors. Our valuation allowance increased approximately \$500,000 during the year ended June 30, 2020.

Note 8 - RETIREMENT PLAN

We sponsor a 401(k) contributory plan (the “Plan”) for the benefit of employees who are at least 21 years of age. At our discretion, we determine the amount of any annual contributions. We elected not to contribute to the Plan for the year ended June 30, 2020.

Note 9 - STOCK PLANS

In 2015, we adopted the 2014 Stock Plan (the “2014 Plan”) to grant equity and equity-linked awards up to a maximum of 6,600,000 shares of common stock. We also have a 2004 Stock Plan (the “2004 Plan”) and a 2006 Stock Plan (the “2006 Plan”). Beginning in January 2015 no stock awards may be granted from either of these earlier plans. If stock option grants are exercised, we expect to issue shares from its currently authorized common shares.

Information with respect to stock options pursuant to the 2004 Plan and 2014 Plan follows (no stock options have been awarded from the 2006 Plan):

	Shares (in thousands)	Weighted- Average Exercise Price	Weighted-Average Remaining Contractual Term
Outstanding - July 1, 2019	5,850	\$.166	
Forfeited	<u>(250)</u>	\$.200	
Outstanding - June 30, 2020	<u>5,600</u>	\$.164	4.7 years
Exercisable at June 30, 2020	<u>5,005</u>	\$.169	4.3 years

All the issued options are ten-year non-qualified stock option grants.

For the years ended June 30, 2020, stock-based compensation expense related to our Stock Plans totaled approximately \$43,000 and is included in operating costs and expenses. In addition, at June 30, 2020, compensation cost related to non-vested stock options not yet recognized totaled approximately \$43,000. This cost is expected to be recognized over a weighted-average period of 20 months.

The number and weighted-average grant date fair value of non-vested stock options is as follows:

	Shares (in thousands)	Weighted-Average Grant Date Fair Value
Non-vested - June 30, 2019	1,007	\$.109
Vested	<u>(412)</u>	\$.105
Non-vested - June 30, 2020	<u>595</u>	\$.080

Note 11 - COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS

Leases

We have a lease for office space which expires August 2021. All of our other leases have terms of less than one year. The future minimum lease payments for the office lease expiring August 2021 is approximately \$19,000 and \$3,000 for the fiscal years ending in June 30, 2021 and 2022, respectively.

Total rent expense charged to operations for the year ended June 30, 2020 was approximately \$121,000. In addition, included in discontinued operations is rent totaling \$23,000.

Software Development and Licensing Agreements

We have contractual arrangements with third-party developers to develop and/or for the rights to exclusively publish and distribute video games. In certain situations, we also maintain an ownership interest in the underlying intellectual property. The payments to third-party developers are generally conditioned upon the achievement by the developers of contractually specified development milestones. Further, these payments to third-party developers typically are advances and, as such, are recoupable against future royalties based on sales of the related game. In certain arrangements, we may also commit to spend specified amounts for marketing support for the game(s) which is (are) to be developed.

Employment Agreements

We have employment agreements with certain executives which provide for annual base compensation, health insurance and other fringe benefits, and contain certain confidentiality and non-compete provisions. Each of the agreements provide that in the event we terminate their employment without cause, we are obligated to pay severance.

In addition, in connection with our acquisition of the assets of Zachtronics LLC, we agreed to establish a bonus pool, which provides for the payment of annual bonuses to the employees hired pursuant to the acquisition based upon a percentage of profits earned from games they develop.

Legal Proceedings

We are subject to claims and litigation arising in the ordinary course of business. We do not believe that any liability from any reasonably foreseeable disposition of such claims and litigation, individually or in the aggregate, would have a material adverse effect on our consolidated financial statements.