



TAPINATOR, INC.

A Delaware Corporation
Incorporated December 9th, 2013

110 West 40th Street, Suite 1902,
New York, NY 10018

Telephone: 914-960-6232
Corporate Website: www.Tapinator.com

SIC Code: 7372

Quarterly Report For the period ending June 30, 2017

The number of shares outstanding of our Common Stock is 59,459,303 as of June 30, 2017

The number of shares outstanding of our Common Stock was 56,959,303 as of December 31, 2016

Indicate by check mark whether the company is a shell company (as defined in Rule 405 of the Securities Act of 1933 and Rule 12b-2 of the Exchange Act of 1934):

Yes: ☐ No: ☒ (Double-click and select "Default Value" to check)

Indicate by check mark whether the company's shell status has changed since the previous reporting period:

Yes: ☐ No: ☒

Indicate by check mark whether a change in control of the company has occurred over this reporting period:

Yes: ☐ No: ☒

The predecessor of Tapinator, Inc. was previously a shell company, therefore the exemption offered pursuant to Rule 144 is not available. Anyone who purchased securities directly or indirectly from us or any of our affiliates in a transaction or chain of transactions not involving a public offering cannot sell such securities in an open market transaction pursuant to a Rule 144 exemption.

Item 1 Exact name of the issuer and the address of its principal executive offices.

1) Name of the issuer

Tapinator, Inc.
Evolution Resources, Inc. (prior to November 4, 2013)

2) Address of the issuer's principal executive offices

Company Headquarters
Address 1: 110 West 40th Street
Address 2: Suite 1902
Address 3: New York, NY 10018
Phone: (914) 930-6232
Email: investor.relations@tapinator.com
Website(s): www.tapinator.com

Item 2 Shares outstanding.

Trading Symbol: TAPM
Exact title and class of securities outstanding: Common Stock
CUSIP: 876037102
Par or Stated Value: \$0.001
Total shares authorized: 150,000,000 as of: 6/30/17
Total shares outstanding: 59,459,303 as of: 6/30/17

Trading Symbol: NA
Exact title and class of securities outstanding: Series A Convertible Preferred Stock
CUSIP: NA
Par or Stated Value: \$0.001
Total shares authorized: 840 as of: 6/30/17
Total shares outstanding: 420 as of: 6/30/17

Trading Symbol: NA
Exact title and class of securities outstanding: Series A-1 Convertible Preferred Stock
CUSIP: NA
Par or Stated Value: \$0.001
Total shares authorized: 1,500 as of: 6/30/17
Total shares outstanding: 1,500 as of: 6/30/17

Item 3 Interim financial statements.

See attached June 30, 2017 Interim Financial Statements at the end of this document.

Item 4 Management's discussion and analysis or plan of operation.

See attached June 30, 2017 Management's Discussion and Analysis of Financial Condition and Results of Operations at the end of this document.

Item 5 Legal proceedings.

There are no current, past, pending or threatened legal proceedings or administrative actions either by or against the Company that could have a material effect on the Company's business, financial condition, or operations and there are no current, past or pending trading suspensions by a securities regulator.

Item 6 Defaults upon senior securities.

The Company has never been in default of the terms of any note, loan, lease, or other indebtedness or financing arrangement requiring the issuer to make payments.

Item 7 Other information.

The Company does not have any item to disclose.

Item 8 Exhibits.

The Company does not have any items to disclose.

Item 9 Certifications.

We, Ilya Nikolayev and Andrew Merkatz, certify that:

1. We have reviewed this quarterly disclosure statement of Tapinator, Inc.;
2. Based on our 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 our 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: August 14, 2017

/s/ Ilya Nikolayev, CEO

/s/ Andrew Merkatz, President & CFO

Quarterly Report

Tapinator, Inc.

Quarter Ended June 30, 2017

Tapinator, Inc.
Quarterly Report
Quarter ended June 30, 2017

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Tapinator, the Tapinator logo and other trademarks or service marks of Tapinator appearing in this report are the property of Tapinator, Inc. Trade names, trademarks and service marks of other companies appearing in this report are the property of their respective holders.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report contains forward looking statements. All statements, other than statements of historical fact, made in this Quarterly Report are forward looking. Examples of forward-looking statements include statements related to industry prospects, our future economic performance including anticipated revenues and expenditures, results of operations or financial position, and other financial items, our business plans and objectives, including our intended product releases, and may include certain assumptions that underlie the forward-looking statements. Forward-looking statements often include words such as “outlook,” “projected,” “intends,” “will,” “anticipate,” “believe,” “target,” “expect,” and statements in the future tense are generally forward-looking.

We have based these forward-looking statements on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. The achievement or success of the matters covered by such forward-looking statements involves significant risks, uncertainties and assumptions. Moreover, we operate in a very competitive and rapidly changing environment and industry. New risks may also emerge from time to time. It is not possible for our management to predict all of the risks related to our business and operations, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this Quarterly Report may not occur and actual results could differ materially and adversely from those anticipated, predicted or implied in the forward-looking statements.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee that the future results, levels of activity, performance or events and circumstances reflected in the forward-looking statements will be achieved or occur, and reported results should not be considered as an indication of future performance. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Except as required by law, we undertake no obligation to update any forward-looking statements for any reason to conform these statements to actual results or to changes in our expectations.

Tapinator, Inc.
Condensed Consolidated Balance Sheets

	<u>June 30, 2017</u> <i>(unaudited)</i>	<u>December 31, 2016</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 200,369	\$ 590,461
Accounts receivable	252,722	326,607
Prepaid expenses	141,594	53,089
Total current assets	<u>594,685</u>	<u>970,157</u>
Property and equipment, net	19,423	20,429
Software development costs, net	1,267,009	1,174,377
Investments	5,000	5,000
Security deposits	22,698	22,698
Total assets	<u>\$ 1,908,815</u>	<u>\$ 2,192,661</u>
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 101,523	\$ 165,744
Due to related parties	54,505	89,697
Deferred Revenue	371,846	85,402
Accrued interest	-	95,760
Senior convertible debenture, net of debt discount	-	158,682
Total current liabilities	<u>527,874</u>	<u>595,285</u>
Senior convertible debenture, net of debt discount	594,209	476,045
Total Liabilities	<u>1,122,083</u>	<u>1,071,330</u>
Commitments and Contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 1,532,500 shares authorized within any series of designation	-	-
Series A convertible preferred stock, \$0.001 par value; 840 and 840 shares designated at June 30, 2017 and December 31, 2016 respectively; 420 and 420 shares issued and outstanding at June 30, 2017 and December 31, 2016, respectively	1	1
Series A-1 convertible preferred stock, \$0.001 par value; 1,500 and 0 shares designated at June 30, 2017 and December 31, 2016 respectively; 1,500 and 0 shares issued and outstanding at June 30, 2017 and December 31, 2016, respectively	2	-
Common stock, \$0.001 par value; 150,000,000 shares authorized; 59,459,303 and 56,959,303 shares issued and outstanding at June 30, 2017 and December 31, 2016, respectively	59,459	56,959
Additional paid-in capital	7,424,193	5,344,918
Accumulated deficit	(6,696,923)	(4,280,547)
Total stockholders' equity	<u>786,732</u>	<u>1,121,331</u>
Total liabilities and stockholders' equity	<u>\$ 1,908,815</u>	<u>\$ 2,192,661</u>

(See accompanying notes to the unaudited condensed consolidated financial statements)

Tapinator, Inc.
Condensed Consolidated Statements of Operations
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Revenue	\$ 620,096	\$ 1,062,474	\$ 1,432,890	\$ 1,911,086
Operating expenses				
Cost of revenue, excluding depreciation and amortization	186,354	323,330	442,723	587,068
Research and development	17,939	22,180	34,989	52,935
Marketing and public relations	156,076	188,862	334,601	219,563
General and administrative	340,938	309,991	678,835	618,443
Amortization of software development costs	180,486	197,584	375,900	386,493
Depreciation and amortization of other assets	5,681	19,833	11,559	38,994
Total expenses	887,474	1,061,780	1,878,607	1,903,496
Operating (loss) Income	(267,378)	694	(445,717)	7,590
Other expenses				
Amortization of debt discount	611,536	323,843	840,627	647,687
Interest expense, net	148,804	81,537	293,478	163,031
Loss on extinguishment of debt	830,001	-	830,001	-
Total other expenses	1,590,341	405,380	1,964,106	810,718
(Loss) before income taxes	(1,857,719)	(404,686)	(2,409,823)	(803,128)
Income taxes	4,400	2,744	6,553	7,119
Net (loss)	<u>\$ (1,862,119)</u>	<u>\$ (407,430)</u>	<u>\$ (2,416,376)</u>	<u>\$ (810,247)</u>
Net (loss) income per share:				
Basic	(\$0.03)	(\$0.01)	(\$0.04)	(\$0.01)
Diluted	(\$0.03)	(\$0.01)	(\$0.04)	(\$0.01)
Weighted average common shares outstanding:				
Basic	59,338,425	56,959,303	58,286,191	57,020,292
Diluted	59,338,425	56,959,303	58,286,191	57,020,292

(See accompanying notes to the unaudited condensed consolidated financial statements)

Tapinator, Inc.
Condensed Consolidated Statement of Stockholders' Equity

	Common Stock		Series A Preferred Stock		Series A-1 Preferred Stock		Additional	Accumulated	
	Shares	Amount	Shares	Amount	Shares	Amount	Paid-In-Capital	Deficit	TOTAL
Balances at December 31, 2016	56,959,303	\$ 56,959	420	\$ 1	-	\$ -	\$ 5,344,918	\$ (4,280,547)	\$ 1,121,331
Common shares issued related to stock purchase agreement	2,500,000	2,500					347,500		350,000
Stock based compensation							61,776		61,776
Shares issued Series A-1 preferred stock related to warrant exchange					1,500	2	659,998		660,000
Debt discount related to conversion feature of convertible debenture and warrant exchange							1,010,001		1,010,001
Net loss								(2,416,376)	(2,416,376)
Balances at June 30, 2017 (unaudited)	59,459,303	\$ 59,459	420	\$ 1	1,500	\$ 2	\$ 7,424,193	\$ (6,696,923)	\$ 786,732

(See accompanying notes to the unaudited condensed consolidated financial statements)

Tapinator, Inc.
Condensed Consolidated Statements of Cash Flows
(*unaudited*)

	Six Months Ended June 30,	
	2017	2016
Cash flows from operating activities:		
Net (loss)	\$ (2,416,376)	\$ (810,247)
Adjustments to reconcile net (loss) to net cash (used in) provided by operating activities:		
Amortization of software development costs	375,900	386,493
Depreciation and amortization of other assets	11,559	38,994
Amortization of debt discount	840,627	647,687
Amortization of original issue discount	186,250	75,790
Loss on extinguishment of debt	830,001	-
Stock based compensation	61,776	-
Accounts receivable	73,885	70,208
Prepaid expenses	(88,505)	32,659
Accounts payable and accrued expenses	(147,450)	(10,190)
Deferred Revenue	286,444	-
Due to related parties	(35,192)	6,863
Net cash (used in) provided by operating activities	<u>(21,081)</u>	<u>438,257</u>
Cash flows from investing activities:		
Capitalized software development costs	(468,532)	(521,149)
Purchase of property, plant and equipment	(3,979)	(9,567)
Net cash (used in) investing activities	<u>(472,511)</u>	<u>(530,716)</u>
Cash flows from financing activities:		
Proceeds from issuance of common stock	350,000	-
Senior convertible debenture principal payment	(234,000)	(560,000)
Payment for senior convertible debenture financing costs	(12,500)	-
Net cash (used in) provided by financing activities	<u>103,500</u>	<u>(560,000)</u>
Net change to cash and cash equivalents	(390,092)	(652,459)
Cash and cash equivalents at beginning of period	<u>590,461</u>	<u>1,487,196</u>
Cash and cash equivalents at end of period	<u><u>\$ 200,369</u></u>	<u><u>\$ 834,737</u></u>
<i>Supplemental disclosure of cash flow information:</i>		
<i>Cash paid for interest</i>	<u>\$ 191,520</u>	<u>\$ 89,600</u>
<i>Cash paid for taxes</i>	<u>\$ 6,550</u>	<u>\$ 7,119</u>
<i>Non-cash investing and financing activities:</i>		
<i>Series A-1 convertible preferred stock issued related to debt extinguishment</i>	<u><u>\$ 660,000</u></u>	<u><u>\$ -</u></u>

(See accompanying notes to the unaudited condensed consolidated financial statements)

Tapinator, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2017
(*unaudited*)

NOTE 1 — ORGANIZATION AND DESCRIPTION OF BUSINESS

Tapinator, Inc. (“Tapinator” or the “Company”) develops and publishes mobile games on the iOS, Google Play, and Amazon platforms. Tapinator's portfolio includes over 300 mobile gaming titles that, collectively, have achieved over 400 million player downloads, including notable games such as ROCKY™, Video Poker Classic, Solitaire Dash, Dice Mage and Burn It Down. Tapinator generates revenues through the sale of branded advertising and via app-store transactions. Founded in 2013, Tapinator is headquartered in New York, with product development teams located in the United States, Germany, Pakistan, Indonesia, Russia and Canada.

The Company was originally incorporated on December 9, 2013 in the state of Delaware. On December 12, 2013, the Company merged with Tapinator, Inc., a Nevada Corporation. The Company was the surviving corporation from this merger. On June 16, 2014, the Company executed a securities exchange agreement with the members of Tapinator LLC, a New York limited liability company, whereby the Company issued 36,700,000 shares of its common stock (representing 80% of its then common stock outstanding after giving effect to the transaction) to the members of Tapinator LLC in exchange for 100% of the outstanding membership interests of Tapinator LLC. The transaction resulted in a business combination and a change of control within its business purpose. For accounting and financial reporting purposes, Tapinator LLC was considered the acquirer and the transaction was treated as a reverse merger.

The Company currently develops two types of games. Tapinator's Rapid-Launch Games are developed and published in significant quantity. These are titles that are built economically and rapidly based on a series of internally developed, expandable and re-useable game engines. These games are currently published under the Tapinator, Tap2Play, TapSim Game Studio, Rizwan Yousuf, and TopTap Games brands. The Company's Full-Featured Games are unique products with high production values and high revenue potential, developed and published selectively based on both original and licensed IP. These titles require significant development investment and have, in the opinion of management, the potential to become well-known and long-lasting, successful mobile game franchises. These games are currently published exclusively under the Tapinator brand.

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Consolidation

The accompanying unaudited condensed consolidated financial statements and related notes have been prepared in conformity with United States generally accepted accounting principles (“GAAP”). The consolidated financial statements include the operations of the Company and its wholly-owned subsidiaries, Tapinator, LLC, Tap2Play, LLC and Tapinator IAF, LLC. All significant intercompany balances and transactions have been eliminated in consolidation. Certain information and footnote disclosures normally included in audited consolidated financial statements prepared in accordance with GAAP have been condensed or omitted. Accordingly, these interim financial statements should be read in conjunction with the Company's audited financial statements and related notes as contained in audited financial statements for the year ended December 31, 2016. In the opinion of management, the interim unaudited condensed consolidated financial statements reflect all adjustments, including normal recurring adjustments, necessary for fair presentation of the interim periods presented. The results of the operations for the three months and six months ended June 30, 2017 are not necessarily indicative of the results of operations to be expected for the full year.

Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amount of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates include assumptions used in the fair value of revenue recognition, platform and advertising fees and related costs of revenue, long-lived assets, stock-based compensation, and the fair value of other equity and debt instruments.

Tapinator, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2017
(unaudited)

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue Recognition

The Company derives revenue from the three gaming platforms on which it currently markets its mobile games in the form of app-store transactions and from various advertising networks in the form of branded advertising placements within its mobile games.

In accordance with Accounting Standards Codification Topic (“ASC”) 605-45, *Revenue Recognition: Principal Agent Considerations*, the Company evaluates its agreements with the gaming platforms and advertising networks to determine whether it is acting as the principal or as an agent when selling its games or when selling premium in-game content or advertisements within its games, which it considers in determining if revenue should be reported gross or net. Key indicators that the Company evaluates to reach this determination include:

- the terms and conditions of the Company’s contracts with the gaming platforms and ad networks;
- the party responsible for determining the type, category and quantity of the methods to generate game revenue;
- whether the Company is paid a fixed percentage of the arrangement’s consideration or a fixed fee for each game, transaction, or advertisement;
- the party which sets the pricing with the end-user, and has the credit and inventory risk; and
- the party responsible for the fulfillment of the game or serving of advertisements and that determines the specifications of the game or advertisement.

Based on the evaluation of the above indicators, the Company has determined that it is generally acting as a principal and is the primary obligor to end-users for its games distributed on the gaming platforms and for advertisements served by the advertising networks and has the contractual right to determine the price to be paid by the player. Therefore, the Company recognizes revenue related to these arrangements on a gross basis, when the necessary information about the gross amounts or platform fees charged, before any adjustments, are made available by the gaming platforms and advertising networks. The Company records the related platform fees and advertising network revenue share as expenses in the period incurred.

The Company recognizes revenue when all of the following conditions are satisfied: there is persuasive evidence of an arrangement; the service is delivered to the player; the collection of fees is reasonably assured; and the amount of fees to be paid by the player is fixed or determinable. For purposes of determining when the service has been provided to the player, we have determined that an implied obligation exists to the paying player to continue displaying the purchased premium in-game content over its estimated life or until it is consumed. Accordingly, we categorize our premium in-game content as either consumable or durable virtual goods. Consumable virtual goods are items consumed at a predetermined time or otherwise have limitations on repeated use, while durable virtual goods are items, such as virtual currency, that remain in the game for as long as the player continues to play. Our revenues from consumable virtual goods have been insignificant since the Company’s formation.

Beginning with the period ended December 31, 2016, we recognize revenue, and the associated costs, from the sale of durable virtual goods ratably over the estimated average playing period of paying players for the applicable game, which represents our best estimate of the average life of durable virtual goods. For the sale of consumable virtual goods, we recognize revenue, and the associated costs, as the goods are consumed. If we do not have the ability to differentiate revenue attributable to durable virtual goods from consumable virtual goods for a specific game, we recognize revenue and the associated costs on the sale of durable and consumable virtual goods for that game ratably over the estimated average period that paying players typically play that game.

Tapinator, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2017
(unaudited)

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Prior to the period ended December 31, 2016, we recognized revenue, and the associated costs, from the sale of all virtual goods at the time of sale. For all fiscal years prior to 2016, we have analyzed the portion of durable virtual goods revenue, and the associated costs, that would have been otherwise deferred using the above revenue recognition policy. We have determined that the effect of such policy would have been immaterial to our reported revenue, net income, and earnings per share results.

On a periodic basis, and no less than annually, we determine the estimated average playing period for paying players by genre across a sample of our games beginning at the time of a player's first purchase in that game and ending on a date when that paying player is no longer playing the game. To determine when paying players are no longer playing a given game, we measure the populations of paying players (the "daily cohort") from the date of their first installation of the game and track each daily cohort to understand the number of players from each daily cohort who played the game after their initial purchase. For titles where we have one or more years of paying players' historical usage data ("Tracked Titles"), we compute a weighted average playing period for paying users using this dataset.

For titles where we have less than one year of paying player data ("New/Untracked Titles"), we use a linear interpolation model on a representative sample of our games within each genre to estimate the average playing period of paying users. Using actual retention data for all players from these games for the period between game installation and up to 90 days thereafter, this data is inputted into a linear interpolation curve to estimate an average playing period for these titles. These calculated curves and their associated one-year average playing periods are mapped against the corresponding curves and associated average one-year playing periods for the Tracked Titles. Based on this mapping, the average playing period of paying users for Tracked Titles is then indexed up or down accordingly, and then applied against the New/Untracked Titles within the sample.

We then compute revenue-based weighted averages of the estimated playing period across all of the games in the sample, by genre, to arrive at the overall weighted average playing period of paying users for each of our major game genres, rounded to the nearest month. As of the fourth quarter of 2016 (our most recent determination date), the estimated weighted average life of our durable virtual goods was 14 months for our Casino / Card games, 2 months for our RPG / Arcade games and 2 months for our Rapid Launch / Simulation games. The estimated weighted average life of our durable virtual goods across all of our games was 7 months as of the fourth quarter of 2016.

While we believe our estimates to be reasonable based on available game player information and based on the disclosed methodologies of larger publicly reporting mobile game companies, we may revise such estimates in the future based on changes in the operational lives of our games, and based on changes in our ability to make such estimates. Any future adjustments arising from changes in the estimates of the lives of these virtual goods would be applied to the then current quarter, and prospectively on the basis that such changes are caused by new information indicating a change in game player behavior patterns compared to historical titles. Any changes in our estimates of useful lives of these virtual goods may result in revenues being recognized on a basis different from prior periods' and may cause our operating results to fluctuate.

Accounts Receivable and Allowance for Doubtful Accounts

The Company monitors outstanding receivables based on factors surrounding the credit risk of specific customers, historical trends, and other information. The allowance for doubtful accounts is estimated based on an assessment of the Company's ability to collect on customer accounts receivable. There is judgment involved with estimating the allowance for doubtful accounts and if the financial condition of the Company's customers were to deteriorate, resulting in their inability to make the required payments, the Company may be required to record additional allowances or charges against revenues. The Company writes-off accounts receivable against the allowance when it determines a balance is uncollectible and no longer actively pursues its collection. As of June 30, 2017 and December 31, 2016, based upon the review of the outstanding accounts receivable, the Company has determined that an allowance for doubtful accounts is not required.

Tapinator, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2017
(unaudited)

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash Equivalents

For purposes of the Statements of Cash Flows, the Company considers all highly liquid investments purchased with an original maturity date of three months or less to be cash equivalents.

Concentrations of Credit Risk

Financial instruments and related items which potentially subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents and trade receivables. The Company places its cash and temporary cash investments with credit quality institutions. At times, such investments may be in excess of the FDIC insurance limit. As of June 30 2017, the total amount exceeding was \$0.

The Company derives revenue from gaming platforms and advertising networks which individually may contribute 10% or more of the Company's revenues in any given year. For the six months ended June 30, 2017, revenue derived from four advertising networks comprised 47% of such period's total revenue. For the six months ended June 30, 2016 revenue derived from four advertising networks comprised 78% of such period's total revenue.

As of June 30, 2017, and December 31, 2016, the receivable balances from four advertising networks comprised 43% and 32% of the Company's total accounts receivable balances, respectively.

Property and Equipment

Property and equipment are stated at cost. When retired or otherwise disposed, the related carrying value and accumulated depreciation are removed from the respective accounts and the net difference, less any amount realized from disposition, is reflected in earnings. Property and equipment are depreciated using the straight-line method over their estimated useful lives as follows:

Computer equipment	3 years
Furniture and fixtures	5 years
Leasehold improvements	remaining term of lease

Software Development Costs

In accordance with ASC 985-20, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed," the Company capitalizes certain costs related to the development of new software products or the enhancement of existing software products for use in our product offerings. These costs are capitalized from the point in time that technological feasibility has been established, as evidenced by a working model or detailed working program design to the point in time that the product is available for general release to customers. Software development costs are amortized on a straight-line basis over the estimated economic lives of the products, beginning when the product is placed into service.

Prior to March 31, 2016, the Company amortized its Rapid-Launch software development costs over 18-months. After an internal re-assessment of estimated economic lives, the Company discovered that the useful lives and expected revenue life of its Rapid-Launch software surpassed 18 months. Therefore, all new Rapid-Launch software development costs incurred after March 31, 2016 are amortized over 36 months. The software development costs incurred prior to March 31, 2016 will continue to amortize under an 18-month basis until they are fully amortized.

Prior to March 31, 2016, the Company generally amortized its Full-Featured Games software development costs over 18 months. After March 31, 2016, the amortization period of its Full-Featured Games software development costs have been determined based on the lesser of their expected revenue lives or the agreement terms with third party IP licensors, typically from 2 to 5 years. The software development costs incurred prior to March 31, 2016 will continue to amortize under an 18-month basis until they are fully amortized.

Tapinator, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2017
(unaudited)

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Software Development Costs (continued)

The Company periodically evaluates whether events or circumstances have occurred that indicate that the remaining useful lives of its capitalized software development costs should be revised or that the remaining balance of such assets may not be recoverable. Software costs incurred prior to establishing technological feasibility are charged to Research and Development expense as incurred.

Impairment of Long-lived Assets

The Company regularly reviews property, equipment, software development costs and other long-lived assets for possible impairment. This review occurs annually or more frequently if events or changes in circumstances indicate the carrying amount of the asset may not be recoverable. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. Based upon management's assessment, there were no indicators of impairment of the Company's property, equipment and software development costs at June 30, 2017.

In general, investments in which the Company owns less than 20 percent of an entity's equity interest or does not hold significant influence over the investee are accounted for under the cost method. Under the cost method, these investments are carried at the lower of cost or fair value. The Company periodically assesses its cost method investments for impairment. If determination that a decline in fair value is other than temporary, the Company will write-down the investment and charge the impairment against operations. At June 30, 2017 and December 31, 2016, the carrying value of its investments totaled \$5,000 and \$5,000, respectively.

Derivative Instrument Liability

The Company accounts for derivative instruments in accordance with ASC 815, *Derivatives and Hedging*, which establishes accounting and reporting standards for derivative instruments and hedging activities, including certain derivative instruments embedded in other financial instruments or contracts, and requires recognition of all derivatives on the balance sheet at fair value, regardless of hedging relationship designation. Accounting for changes in fair value of the derivative instruments depends on whether the derivatives qualify as hedge relationships and the types of relationships designated are based on the exposures hedged. At June 30, 2017 and December 31, 2016, the Company did not have any derivative instruments that were designated as hedges.

Fair Value of Financial Instruments

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. Assets and liabilities that are measured at fair value are reported using a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy maximizes the use of observable inputs and minimizes the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 – Unadjusted quoted prices in active markets that are accessible at the measurement date of identical, unrestricted assets or liabilities.
- Level 2 – Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability; and
- Level 3 – Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

As of June 30, 2017, and December 31, 2016, the Company did not identify any non-recurring assets and liabilities that are required to be presented in the balance sheets at fair value in accordance with ASC 825, *Financial Instruments*.

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NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cost of Revenue (excluding amortization of software development costs)

Cost of revenue includes primarily platform and advertising network fees, licensing costs and hosting fees. The Company, along with all mobile application publishers, is required to pay platform fees to Apple, Google and Amazon equal to approximately 30% of gross revenue. The Company is also required to pay a revenue share of approximately 30% to advertising networks and similar service providers.

Stock-Based Compensation

The Company measures the fair value of stock-based compensation issued to employees and non-employees using the stock price observed in the arms-length private placement transaction nearest the measurement date (for stock transactions), or the fair value of the award (for non-stock transactions), which are considered to be more reliably determinable measures of fair value than the value of the services being rendered. The measurement date is the earlier of (1) the date at which commitment for performance by the counterparty to earn the equity instruments is reached, or (2) the date at which the counterparty's performance is complete.

Basic and Diluted Net Income (Loss) per Share Calculations

Net income (loss) per share is shown under two calculations -- basic and diluted. Basic net income (loss) per share is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding during the period available. Diluted net income (loss) per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. For the quarter ended June 30, 2017, potentially dilutive securities excluded from the computation of basic and diluted net (loss) per share include 10,800,000 potentially convertible common shares related to the Company's Senior Secured Convertible Debenture, 1,680,000 potentially convertible common shares related to the Company's Series A Preferred Stock, 6,000,000 potentially convertible shares related to the Company's Series A-1 Preferred Stock, 5,050,000 Common Stock Options and 3,500,000 Common Stock Warrants.

For the six months ended June 30, 2016, potentially dilutive securities excluded from the computation of basic and diluted net (loss) per share include 10,926,829 potentially convertible shares related to the senior secured convertible debenture, 500,000 options and 21,853,658 common stock warrants.

Recent Accounting Pronouncements

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350). This ASU eliminates Step 2 from the goodwill impairment test. Under the new guidance, an entity should perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value. Additionally, this ASU eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. The amendments in this ASU are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years, and is applied on a prospective basis. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. While we are currently evaluating the impact of the adoption of this ASU, we do not believe that the adoption of this guidance will have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases. This new guidance requires lessees to recognize a right-of-use asset and a lease liability for virtually all leases (other than leases that meet the definition of a short-term lease). The liability will be equal to the present value of lease payments. The asset will be based on the liability, subject to adjustment, such as for initial direct costs. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). Classification will be based on criteria that are largely similar to those applied in current lease accounting. This

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NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

update is effective for annual periods, and interim periods within those years, beginning after December 15, 2018. This new guidance must be adopted using a modified retrospective approach whereby lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. We are currently evaluating the impact of adopting this update on our Consolidated Financial Statements, which will consist primarily of a balance sheet gross up of our operating leases, mostly for office space.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606) . Under the new standard, revenue is recognized when a customer obtains control of promised goods or services and is recognized in an amount that reflects the consideration, which the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The FASB recently issued several amendments to the standard, including clarifications on disclosure of prior-period performance obligations and remaining performance obligations. The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method). The new standard is effective for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted for annual reporting periods beginning after December 15, 2016. The Company will adopt the new standard effective December 1, 2018. We are currently evaluating the impact of adopting this standard on our Consolidated Financial Statements.

Management does not believe that any other recently issued, but not yet effective, accounting standards if currently adopted would have a material effect on the accompanying consolidated financial statements.

NOTE 3 — PROPERTY AND EQUIPMENT

Property and equipment consisted of the following as of June 30, 2017 and December 31, 2016:

	June 30, 2017	December 31, 2016
Leasehold improvements	\$ 2,435	\$ 2,435
Furniture and fixtures	10,338	8,238
Computer equipment	24,285	22,406
Property and equipment cost	37,058	33,079
Less: accumulated depreciation	(17,635)	(12,650)
Property and equipment, net	<u>\$ 19,423</u>	<u>\$ 20,429</u>

During the six months ended June 30, 2017 and June 30, 2016, depreciation expense was \$4,985 and \$3,408, respectively.

NOTE 4—CAPITALIZED SOFTWARE DEVELOPMENT

Capitalized software development costs at June 30, 2017 and December 31, 2016 were as follows:

	June 30, 2017	December 31, 2016
Software development cost	\$ 2,910,157	\$ 2,441,625
Less: accumulated amortization (a)	(1,643,148)	(1,267,248)
Capitalized software development cost, net	<u>\$ 1,267,009</u>	<u>\$ 1,174,377</u>

(a) During the six months ended June 30, 2017 and June 30, 2016, amortization expense related to capitalized software was \$375,900 and \$386,493, respectively.

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NOTE 5 — RELATED PARTY TRANSACTIONS

The Company utilizes the services of an affiliated entity of a major shareholder for the development of certain of its mobile games. Amounts incurred by the Company for such development services, which were primarily attributed to capitalized software development costs, for the six months ended June 30, 2017 and June 30, 2016 were \$266,320 and \$330,049, respectively. As of June 30, 2017, and December 31, 2016, the Company had balances due to related parties related primarily to the software development services of \$54,505 and \$89,697, respectively

NOTE 6 — SENIOR SECURED CONVERTIBLE DEBENTURE

In July 2016, the Company and the Holder entered into an agreement (the “2016 Exchange Agreement”) to amend and refinance the terms of the \$2,240,000 8% Original Issue Discount Senior Secured Convertible Debenture (the “2015 Debenture”) originally issued to the Holder in June, 2015.

In connection with the 2015 Debenture, the Company and Holder entered into that certain Securities Purchase Agreement, dated June 19, 2015 (the “Purchase Agreement”) pursuant to which the Company issued to the Holder the following (i) the 2015 Debenture which was convertible into shares of the Company’s common stock at a price per share of \$.205, (ii) Series A Common Stock purchase warrants (the “Series A Warrants”) to purchase up to 10,926,829 shares of common stock with an exercise price of \$.30 and (iii) Series B Common Stock purchase warrants (the “Series B Warrants”) to purchase up to 10,926,829 shares of common stock with an exercise price of \$.30 (collectively, the terms of which are referred to herein as the “2015 Financing”). Immediately prior to the 2016 Exchange Agreement, the Company owed cash payments to the Holder of \$560,000 on October 1, 2016 and \$1,120,000 on January 1, 2017 under the 2015 Debenture.

Pursuant to the 2016 Exchange Agreement, the following material terms of the Original Financing were amended, altered and/or ratified (collectively, the terms of which are referred to herein as the “2016 Financing”): (i) the 2015 Debenture was exchanged in its entirety for the issuance of a new 8% Original Issue Discount Senior Secured Convertible Debenture with an original principal amount of \$2,394,000 and an increased conversion price of \$0.25 (the “2016 Debenture”), (ii) the issuance of 420 shares of Series A Convertible Preferred Stock (the “Series A Preferred Stock”) as further described by the Certificate of Designation of Preferences, Rights and Limitations of Series A Convertible Preferred Stock which may be converted into 1,680,000 shares of Company’s common stock, (iii) the extension of the maturity date of the Series A Warrants from June 22, 2020 until July 28, 2021, (iv) the cancellation of the Series B Warrants in their entirety, (v) the ratification of the Security Agreement executed by the Company with respect to all of its assets (as required by the initial Purchase Agreement and 2015 Debenture) as continued collateral for the 2016 Debenture as well as the ratification of the Subsidiary Guarantee and Pledge and Security Agreement as such agreements are referenced in the Purchase Agreement and Exchange Agreement, and (vi) the creation of a new right for the Holder, subject to the written consent of the Company, for a \$2,100,000 cash investment in the Company with identical terms to the 2016 Financing.

In June 2017, the Company and the holder of its Senior Secured Convertible Debenture (the “Holder”) entered into an amendment agreement (the “2017 Amended Agreement”) to amend and refinance the terms of the \$2,394,000 8% Original Issue Discount Senior Secured Convertible Debenture (the “2016 Debenture”) originally issued to the Holder in July, 2016.

According to the 2017 Amendment Agreement, the Company prepaid the Holder a portion of the outstanding principal on the 2016 Debenture in the amount of \$234,000 and all of the accrued interest on the 2016 Debenture through June 30, 2017 in the amount of \$191,520. Following such payments, the remaining principal amount of the Holder’s 2017 Amended Debenture was \$2,160,000. In addition, the Company and the Holder agreed to reduce the Conversion Price from \$0.25 in the 2016 Debenture to \$0.20 in the Amended Debenture.

The 2017 Amendment Agreement is due on July 31, 2018, and the Company shall pay interest to the Holder on the aggregate unconverted and then outstanding principal amount of this debenture at the rate of 8% per annum, payable on each December 31, March 31, July 31, and October 31, thereafter, beginning on December 31, 2017.

In June 2017, the Company and Holder also entered into an exchange agreement (the “2017 Exchange Agreement”) to exchange the existing 10,926,829 shares of Series A Common Stock purchase warrants (the “Series A Warrants”) for

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NOTE 6 — SENIOR SECURED CONVERTIBLE DEBENTURE (continued)

1,500 shares of Series A-1 Convertible Preferred Stock (the “Series A-1 Preferred Stock”) as further described by the Certificate of Designation of Preferences, Rights and Limitations of Series A-1 Convertible Preferred Stock which may be converted into 6,000,000 shares of the Company’s common stock.

The 2017 Amendment Agreement and the Series A and Series A-1 Preferred Stock contain anti-dilution protection such that the conversion and exercise price, respectively, will be adjusted for any subsequent equity transactions with an effective price per share lower than the conversion price, but not lower than \$0.10 per share.

During the six months ended June 30, 2017 and 2016, amortization of the debt discount related to the Senior Secured Convertible Debentures was \$846,627 and \$647,687, respectively. During the six months ended June 30, 2017 and 2016, amortization of the original issue discount was \$186,250 and \$75,790, respectively. As of result of the 2017 Amendment Agreement, the Company recorded a loss of \$830,001 related to the debt original debt extinguishment for the six months ended June 30, 2017.

Senior secured convertible debenture payable as of June 30, 2017, and December 31, 2016 were comprised of the following:

	<u>June 30, 2017</u>	<u>December 31, 2016</u>
Principal balance outstanding	\$ 2,160,000	\$ 2,394,000
Less:		
Debt discount – beneficial conversion feature	(1,221,191)	(1,221,818)
Debt discount – original issue discount	(332,993)	(519,273)
Debt discount – financing costs	(11,607)	(18,182)
Principal balance outstanding, net	<u>594,209</u>	<u>634,727</u>
Less current portion	<u>-</u>	<u>158,682</u>
Long term portion	<u>594,209</u>	<u>476,045</u>

NOTE 7 — STOCKHOLDERS’ EQUITY

At June 30, 2017, the authorized capital of the Company consisted of 150,000,000 shares of common stock, par value \$0.001 per share, and 1,532,500 shares of blank check preferred stock, par value \$0.001 per share.

In June, 2017, the Company entered into a Stock Purchase Agreement with an individual investor for the purchase of 2,000,000 shares of the Company’s common stock for an aggregate purchase price of \$200,000. In connection with the financing, the Company also issued to the investor a warrant, which has a term of three years and shall enable the investor to purchase up to an additional 2,500,000 shares of the Company’s common stock at an exercise price of \$.20 per share.

In February, 2017, the Company entered into a Stock Purchase Agreement with an individual investor for the purchase of 500,000 shares of the Company’s common stock for an aggregate purchase price of \$150,000, or \$0.30 per share, which will be payable in two tranches. In connection with the financing, the Company also issued to the investor two warrants. Each warrant has a term of three years and each warrant shall enable the investor to purchase up to an additional 500,000 shares of the Company’s common stock at an exercise price of \$.30 per share and \$.36 per share, respectively.

The Company issued 300,000 shares of restricted Common Stock, valued at \$57,000, pursuant to an investor relations consulting agreement dated August 6, 2015. On March 14, 2016, the agreement was cancelled and 150,000 shares of the Company’s common stock valued at \$28,500 were returned to the Company at which time the shares were cancelled.

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NOTE 8 — COMMON STOCK WARRANTS

During the six months ended June 30, 2017, the company granted warrants in connection with the Stock Purchase Agreements described in Note 7. The warrant terms are 3 years expiring on February, 2020 and May, 2020.

	2017		
	Number of Common Stock Warrants	Weighted average exercise price	Weighted average life (years)
Outstanding, January 1, 2017	10,926,829	\$ 0.30	4.58
Granted	3,500,000	0.24	3.00
Exercised	-	-	-
Canceled	10,926,829	0.30	3.93
Outstanding, June 30, 2017	<u>3,500,000</u>	<u>\$ 0.24</u>	<u>2.85</u>

NOTE 9—OPTIONS

On May 11, 2017 and pursuant to the 2015 Equity Incentive Plan, the Company granted executive officers, directors and employees options to purchase 4,500,000 shares of the Company's common stock at an exercise price equal to \$0.11 per share. Such option shall vest in twelve quarterly installments of 375,000 shares at the end of each quarterly anniversary commencing on June 30, 2017, contingent upon the grantee's continual employment or service with the Company as of each vesting installment date. Total stock-based compensation related to this option grant was \$25,000 during the six months ended June 30, 2017.

In January 2016 and pursuant to the 2015 Equity Incentive Plan, the Company granted a non-executive member of the Company's Board of Directors an option to purchase 300,000 shares of the Company's common stock at an exercise price equal to \$0.33 per share. Such option shall vest in eight quarterly installments of 37,500 shares at the end of each quarterly anniversary commencing on March 31, 2016, contingent upon the grantee's continual service as a member of the Board of Directors as of each vesting installment date. Total stock-based compensation related to this option grant was \$24,745 during the six months ended June 30, 2017.

In May 2016 and pursuant to the 2015 Equity Incentive Plan, the Company granted an executive officer an option to purchase 250,000 shares of the Company's common stock at an exercise price equal to \$0.1925 per share. Such option shall vest in eight quarterly installments of 31,250 shares at the end of each quarterly anniversary commencing on August 31, 2016, contingent upon the grantee's continual employment by the Company as of each vesting installment date. Total stock-based compensation related to this option grant was \$12,031 during the six months ended June 30, 2017.

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NOTE 9—OPTIONS (continued)

The fair value of the stock options issued in 2017 was determined using the Black Scholes option pricing model with the following assumption: dividend yield: 0%; volatility: 304.61%; risk free rate: 2.39%; term 10 years.

	2017		
	Number of Options	Weighted average exercise price	Weighted average life (years)
Outstanding, January 1, 2017	550,000	\$ 0.27	9.23
Granted	4,500,000	0.11	10.00
Exercised	-	-	-
Expired	-	-	-
Outstanding, June 30, 2017	5,050,000	\$ 0.13	9.75
Exercisable, June 30, 2017	725,000	\$ 0.19	9.31

NOTE 10—SUBSEQUENT EVENTS

On July 26, 2017 the Company announced that its common shares have begun trading on the OTC Markets Group's OTCQB® Venture Market and will continue to trade under the ticker symbol "TAPM".

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the accompanying notes included elsewhere in this Quarterly Report. The following discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Quarterly Report, particularly in "Special Note Regarding Forward-Looking Statements." The forward-looking statements included in this Quarterly Report are made only as of the date hereof.

Overview

This overview provides a high-level discussion of our operating results and some of the trends that affect our business. We believe that an understanding of these trends is important to understand our financial results for the period ended June 30, 2017 and period ended June 30, 2016. This summary is not intended to be exhaustive, nor is it intended to be a substitute for the detailed discussion and analysis provided elsewhere in this report, including our unaudited condensed consolidated financial statements and accompanying notes.

Tapinator, Inc. develops and publishes free to play ("F2P") mobile games for smartphones and tablets on the iOS, Google Play, and Amazon platforms. Tapinator's portfolio includes over 300 mobile gaming titles that, collectively, have achieved over 400 million player downloads, including notable games such as ROCKY™, Video Poker Classic, Solitaire Dash, Dice Mage and Burn It Down. Tapinator generates revenues through the sale of branded advertisements and via consumer app-store transactions.

The Company currently develops two types of games. Tapinator's Rapid-Launch Games are developed and published in significant quantity. These are titles that are built economically and rapidly based on a series of internally developed, expandable and re-useable game engines. These games are currently published under the Tapinator, Tap2Play, and TapSim Game Studio brands. The Company's Full-Featured Games are unique products with high production values and high revenue potential, developed and published selectively based on both original and licensed IP. These titles require significant development investment and have, in the opinion of management, the potential to become well-known and long-lasting, successful mobile game franchises. These games are currently published exclusively under the Tapinator brand.

Rapid-Launch Games: We define a Rapid-Launch Game as a product that is built on top of one of our internally developed Rapid-Launch Game engines. To date, we have developed engines (and launched approximately 300 Rapid-Launch titles) within the following game genres: parking, driving, stunts, shooters, fighting, animal sims, career sims and racing. For example, we have created a proprietary parking simulation engine and have used this to launch car, truck, limousine, ambulance, and other types of vehicle parking simulation games. These games are monetized primarily through branded advertisements which are typically sold via third-party advertising networks and trafficked via third-party ad mediation software installed within the games. These games are marketed primarily through cross-promotion within our existing Rapid-Launch Game network and via various app-store optimization ("ASO") strategies.

Full-Featured Games: We define a Full-Featured Game as a product that is designed and engineered on a completely custom basis (i.e. not based on an existing game engine), and one that contains unique components of gameplay, systems, themes, IP or some combination thereof. Full-Featured Games require significant development investment and have, in the opinion of management, the potential to become well-known and long-lasting successful mobile game franchises. To date, the Company has developed and/or published approximately 15 Full-Featured Games including notable titles such as: ROCKY™, Video Poker Classic, Solitaire Dash, Dice Mage, and Burn It Down. Eleven of these games have been featured as "Best New Games" or "New Games We Love" by Apple on the iOS platform, and a subset of these games have also been featured by the Google Play and Amazon App Stores. These games are marketed primarily through app-store feature placement and through paid marketing channels in cases where the Company believes that a game's average player Lifetime Value ("LTV") exceeds that of the game's average player customer acquisition cost. Full-Featured Games are monetized primarily via consumer app-store transactions.

Strategy

In early 2017, we announced a strategic shift to focus more of our investment and management resources into our Full-Featured Games business. We believe the potential size, quality and sustainability of revenues and earnings from the Full-Featured Games business is significantly greater than that of our existing Rapid-Launch Games business. Our goal in terms of our Full-Featured Games is to create franchise-type titles that have product lifespans of at least five years. In order to accomplish this, we believe that we need to achieve player LTVs that exceeds customer acquisition cost, at scale. To date, the Company has been able to achieve this, at certain player volumes, for two products: “Video Poker Classic” and “Solitaire Dash.”

Current Outlook

As demonstrated by our strategic shift, we are confident in our ability to continue to drive strong year-over-year growth in key operating and financial metrics within our Full-Featured Games business. This growth is expected to be derived from a combination of existing games such as Video Poker Classic and Solitaire Dash, games that we have recently launched (following the end of the second quarter) such as Big Sport Fishing 2017 and Dice Mage 2, and games that we plan to launch later this year such as Divide & Conquer and Fusion Heroes.

In terms of our Rapid-Launch Games business, we have experienced declines in our second quarter year-over-year results in key operating and financial metrics, and we expect to show declines in our third quarter year-over-year results as well. These declines are a result of low success rates of Rapid-Launch Games launched during the first half of this year, combined with challenging year-over-year comparisons due to a significant but un-sustained strengthening in the 2016 comparative periods. We believe the slowdown in the Rapid-Launch Games business has abated, however, as third quarter key operating and financial metrics are currently trending to show modest sequential increases in key operating and financial metrics. We are cautiously encouraged by the launch performance of two recent Rapid-Launch Games in particular, Fidget Spinner Superhero and Scary Shark Evolution 3D.

We are not, at this time, offering specific guidance for fiscal 2017 but we plan to do so when we are able to predict our annual results with significant certainty. However, we continue to remain confident in our ability to achieve the three-year annualized bookings growth target of 30%, as communicated in our annual shareholder letter that we released in February 2017.

Key Metrics

We regularly review a number of metrics, including the following key operating and financial metrics, to evaluate our business, measure our performance, identify trends in our business, prepare financial projections and make strategic decisions.

Key Operating Metrics

We manage our business by tracking various non-financial operating metrics that give us insight into user behavior in our games. The three metrics that we use most frequently are Daily Active Users (“DAUs”), Monthly Active Users (“MAUs”) and Average Bookings Per User (“ABPU”).

DAUs. We define DAUs as the number of individuals who played a particular smartphone game on a particular day. An individual who plays two different games on the same day is counted as two active users for that day when we aggregate DAU across games. In addition, an individual who plays the same game on two different devices during the same day (e.g., an iPhone and an iPad) is also counted as two active users for each such day when we average or aggregate DAU over time. Average DAU for a particular period is the average of the DAUs for each day during that period. We use DAU as a measure of player engagement with the titles that our players have downloaded.

MAUs. We define MAUs as the number of individuals who played a particular smartphone game in the month for which we are calculating the metric. An individual who plays two different games in the same month is counted as two active users for that month when we aggregate MAU across games. In addition, an individual who plays the same game on two different devices during the same month (e.g., an iPhone and an iPad) is also counted as two active users for each such month when we average or aggregate MAU over time. Average MAU for a particular period is the

average of the MAUs for each month during that period. We use the ratio between DAU and MAU as a measure of player retention.

ABPU. We define ABPU as our total bookings in a given period, divided by the number of days in that period, divided by, the average DAUs during the period. We believe that ABPU provides useful information to investors and others in understanding and evaluating our results in the same manner as our management and board of directors. We use ABPU as a measure of overall monetization across all of our players through the sale of virtual goods and advertising.

Key Financial Metrics

Bookings. Bookings is a non-GAAP financial measure that is equal to revenue recognized during the period plus the change in deferred revenue during the period. We record the sale of virtual goods as deferred revenue and then recognize that revenue over the estimated average life of the purchased virtual goods or as the virtual goods are consumed. Bookings, as opposed to revenue, is the fundamental top-line metric we use to manage our business, as we believe it is a useful indicator of the sales activity in a given period. Over the long term, the factors impacting our bookings and revenue are the same. However, in the short term, there are factors that may cause revenue to exceed or be less than bookings in any period.

We use bookings to evaluate the results of our operations, generate future operating plans and assess the performance of our company. While we believe that this non-GAAP financial measure is useful in evaluating our business, this information should be considered as supplemental in nature and is not meant as a substitute for revenue recognized in accordance with U.S. GAAP. In addition, other companies, including companies in our industry, may calculate bookings differently or not at all, which reduces its usefulness as a comparative measure.

Trends in Key Operating Metrics

<u>All Games</u>	Three Months Ended			
	2017		2016	
	June 30	March 31	June 30	March 31
	(In thousands)			
Average DAUs	627	890	1,074	743
Average MAUs	11,094	15,882	18,305	11,737
ABPU	0.01	0.01	0.01	0.01

The decrease in average DAU and MAU for the three months ended June 30, 2017 as compared to the three months ended June 30, 2016 was primarily related to a significant and rapid strengthening of our Rapid-Launch Games business that we experienced in the second and third quarters of 2016, but that has not since been sustained. This strengthening occurred across our entire Rapid-Launch Games portfolio, but was driven by the success of a number of specific titles launched in late 2015 and early 2016 including *Crocodile Attack 2016*, *Hoverboard Stunts Hero*, and *Multi-Story Car Parking 3D*.

The increase in average DAU and MAU for the three months ended March 31, 2017 as compared to the three months ended March 31, 2016 was primarily related to the continued growth in the size of our Rapid-Launch Games library during the period, including very strong performance from *Legendary Stuntman Run*, a new game launched in January 2017, combined with solid continued performance from certain older Rapid-Launch Games such as *Crocodile Attack 2016*, *Extreme Car Stunts 3D* and *Multi-Story Car Parking 3D*. Growth in the size of our Full-Featured Games portfolio also contributed to the DAU and MAU increase for the comparative periods, led by the April 2016 launch of Video Poker Classic and the December 2016 launch of ROCKY™.

The ABPU remained unchanged for the three months ended June 30, 2017 and March 31, 2017 as compared to the three months ended June 30, 2016 and March 31, 2016.

<u>Rapid-Launch Games</u>	Three Months Ended			
	2017		2016	
	June 30	March 31	June 30	March 31
	(In thousands)			
Average DAUs	602	869	1,066	830
Average MAUs	10,880	15,653	18,203	11,848
ABPU	0.01	0.01	0.02	0.01

The decrease in average DAU and MAU for the three months ended June 30, 2017 as compared to the three months ended June 30, 2016 was primarily related to a significant and rapid strengthening of our Rapid-Launch Games business that we experienced in the second and third quarters of 2016, but that has not since been sustained. This strengthening occurred across our entire Rapid-Launch Games portfolio, but was driven by the success of a number of specific titles launched in late 2015 and early 2016 including *Crocodile Attack 2016*, *Hoverboard Stunts Hero*, and *Multi-Story Car Parking 3D*.

The ABPU within our Rapid-Launch Games decreased for the three months ended June 30, 2017 as compared to the three months ended June 30, 2016, driven by a reduction in both advertising prices (“CPM’s” or “Cost Per Thousand Impressions”) and player engagement (impressions per DAU) during the relative periods.

The increase in average DAU and MAU for the three months ended March 31, 2017 as compared to the three months ended March 31, 2016 was primarily related to the continued growth in the size of our Rapid-Launch Games library during the period, including very strong performance from *Legendary Stuntman Run*, a new game launched in January 2017, combined with solid continued performance from certain older Rapid-Launch Games such as *Crocodile Attack 2016*, *Extreme Car Stunts 3D* and *Multi-Story Car Parking 3D*.

The ABPU within our Rapid-Launch Games remained unchanged for the three months ended March 31, 2017 as compared to the three months ended March 31, 2016.

<u>Full-Featured Games</u>	Three Months Ended			
	2017		2016	
	June 30	March 31	June 30	March 31
	(In thousands)			
Average DAUs	25	22	10	10
Average MAUs	214	451	156	164
ABPU	0.14	0.15	0.09	0.06

The increase in average DAU and MAU for the three months ended June 30, 2017 as compared to the three months ended June 30, 2016 was primarily related to growth in our Full-Featured Games portfolio, and specifically from growth in Video Poker Classic, ROCKY™, and Solitaire Dash.

The increase in average DAU and MAU for the three months ended March 31, 2017 as compared to the three months ended March 31, 2016 was primarily related to growth in our Full-Featured Games portfolio, and specifically from growth in Video Poker Classic, ROCKY™, and Solitaire Dash.

The increase in our Full-Featured Games’ ABPU for the three months ended June 30, 2017 and March 31, 2017 as compared to the three months ended June 30, 2016 and March 31, 2016 was primarily related to strong player monetization performance achieved within both our Video Poker Classic and Solitaire Dash games.

Trends in Key Financial Metrics

Bookings Results

Bookings for the three months ended June 30, 2017 was \$750 thousand, a 29% decrease compared to the three months ended June 30, 2016, in which we reported bookings of \$1.06 million. The decrease was caused by a 54% bookings decrease in our Rapid Launch Games business, which was partially offset by a 222% increase in our smaller, Full-Featured Games business.

Bookings for the six months ended June 30, 2017 was \$1.72 million, a 10% decrease compared to the six months ended June 30, 2016, in which we reported bookings of \$1.91 million. The decrease was caused by a 36% bookings decrease in our Rapid Launch Games business, which was partially offset by a 332% increase in our smaller, Full-Featured Games business.

	Three Months Ended		Six Months Ended	
	Jun. 30, 2017	Jun. 30, 2016	Jun. 30, 2017	Jun. 30, 2016
Bookings by Game Type	(In thousands)			
Full-Featured	\$294	\$79	\$583	\$135
Rapid-Launch	456	984	1,135	1,776
Total	\$750	\$1,063	\$1,718	\$1,911

Our Full-Featured Games' bookings increased \$215 thousand, or 272%, from \$79 thousand for the three months ended June 30, 2016 to \$294 thousand for the three months ended June 30, 2017. The increase in Full-Featured bookings is attributable primarily to growth in player engagement and monetization within Video Poker Classic, and to the successful launches of Solitaire Dash and ROCKY™ between the comparable periods.

Our Rapid-Launch Games' bookings decreased \$528 thousand, or 54%, from \$984 thousand for the three months ended June 30, 2016 to \$456 thousand for the three months ended June 30, 2017. The decrease in bookings is attributable primarily to a decrease in DAUs and ABPU across our Rapid-Launch Games portfolio.

Our Full-Featured Games' bookings increased 448 thousand, or 332%, from \$135 thousand for the six months ended June 30, 2016 to \$583 thousand for the six months ended June 30, 2017. The increase in Full-Featured bookings is attributable primarily to growth in player engagement and monetization within Video Poker Classic, and to the successful launches of Solitaire Dash and ROCKY™ between the comparable periods.

Our Rapid-Launch Games' bookings decrease \$641 thousand, or 36%, from \$1.18 million for the six months ended June 30, 2016 to \$1.14 million for the six months ended June 30, 2017. The decrease in bookings is attributable primarily to a decrease in DAUs and ABPU across our Rapid-Launch Games portfolio.

The following table presents a reconciliation of bookings to revenue for each of the periods presented (in thousands):

	Three Months Ended		Six Months Ended	
	Jun. 30, 2017	Jun. 30, 2016	Jun. 30, 2017	Jun. 30, 2016
	(In thousands)			
Bookings	\$750	\$1,063	\$1,719	\$1,911
Change in deferred revenue	(130)	0	(286)	0
Revenue	\$620	\$1,063	\$1,433	\$1,911

Limitations of Bookings

- Bookings does not reflect that we defer and recognize mobile game revenue over the estimated life of durable virtual goods; and
- other companies, including companies in our industry, may calculate bookings differently or not at all, which reduces their usefulness as a comparative measure.

Because of these limitations, you should consider bookings along with other financial performance measures, including revenue, net income (loss) and our other financial results presented in accordance with U.S. GAAP.

Results of Operations

The following sections discuss and analyze the changes in the significant line items in our statements of operations for the comparison periods identified.

Comparison of the Three Months Ended June 30, 2017 and 2016

Revenue

	Three Months Ended June 30,	
	2017	2016
Revenue by Type	(In thousands)	
Consumer App-store Transactions	\$ 162	\$ 176
Advertising/Other	458	887
Total	<u>\$ 620</u>	<u>\$ 1,063</u>

Our revenue decreased \$443 thousand, or 42%, from \$1.06 million for the three months Ended June 30, 2016 to \$620 thousand for the three months ended June 30, 2017. The decrease in revenue is attributable primarily to a decrease in advertising related bookings within our Rapid-Launch Games business and it was partially offset by an increase in consumer app-store transaction bookings within our Full-Featured Games business.

	Three Months Ended June 30,	
	2017	2016
Revenue by Game Type	(In thousands)	
Full-Featured	\$ 162	\$ 79
Rapid-Launch	458	984
Total	<u>\$ 620</u>	<u>\$ 1,063</u>

Our Full-Featured Games' revenue increased \$83 thousand, or 105%, from \$79 thousand for the three months ended June 30, 2016 to \$162 thousand for the three months ended June 30, 2017. The increase in Full-Featured revenue is attributable primarily to growth in player engagement and monetization within Video Poker Classic, and to the successful launches of Solitaire Dash and ROCKY™ between the comparable periods.

Our Rapid-Launch Games' revenue decreased \$526 thousand, or 53%, from \$984 thousand for the three months ended June 30, 2016 to \$458 thousand for the three months ended June 30, 2017. The decrease in revenue is attributable primarily to a decrease in advertising related bookings stemming from a decrease in DAUs and ABPU across our Rapid-Launch Games portfolio.

Cost of Revenue

	Three Months Ended June 30,	
	2017	2016
	(In thousands)	
Platform Fees	\$ 176	\$ 319
Licensing + Royalties	8	2
Hosting	2	2
Total	\$ 186	\$ 323

Our cost of revenue decreased \$137 thousand, or 42%, from \$323 thousand in the three months ended June 30, 2016 to \$186 thousand in the three months ended June 30, 2017. This decrease was primarily due to a decrease in corresponding revenue during the same period.

Research and Development Expenses

	Three Months Ended June 30,	
	2017	2016
	(In thousands)	
Research and development	\$ 18	\$ 22
Percentage of revenue	3%	2%

Our research and development expenses decreased \$4 thousand, or 18%, from \$22 thousand in the three months ended June 30, 2016 to \$18 thousand in the three months ended June 30, 2017. The decrease in research and development costs was primarily due to a decrease in revenue share associated with some of our older games.

Marketing Expenses

	Three Months Ended June 30,	
	2017	2016
	(In thousands)	
Marketing and public relations	\$ 156	\$ 189
Percentage of revenue	25%	18%

Our marketing expenses decreased \$33 thousand, or 17%, from \$189 thousand in the three months ended June 30, 2016 to \$156 thousand in the three months ended June 30, 2017. The decrease in 2017 was primarily due to higher marketing expenditures related to the initial launch campaign for Video Poker Classic during the second quarter of 2016.

General and Administrative Expenses

	Three Months Ended June 30,	
	2017	2016
	(In thousands)	
General and administrative	\$ 341	\$ 310
Percentage of revenue	55%	29%

Our general and administrative expenses increased \$31 thousand, or 10%, from \$310 thousand in the three months ended June 30, 2016 to \$341 thousand in the three months ended June 30, 2017. The increase in general and administrative expenses was primarily due to an increase in personnel and related expenditures during the comparable periods.

Amortization of capitalized software development

		Three Months Ended June 30,	
		2017	2016
		(In thousands)	
Amortization of capitalized software development	\$	180	\$ 198
Percentage of revenue		29%	19%

Our Amortization of capitalized software development decreased \$18 thousand or 9% from \$198 thousand in the three months ended June 30, 2016 to \$180 thousand in the three months ended June 30, 2017. The decrease in amortization of capitalized software development was attributable to a reduction in development expenditures relating to our Rapid-Launch Games in 2017.

Comparison of the Six Months Ended June 30, 2017 and 2016

Revenue

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Revenue by Type			
Consumer App-store Transactions	\$	507	\$ 315
Advertising/Other		926	1,596
Total	\$	1,433	\$ 1,911

Our revenue decreased \$478 thousand, or 25%, from \$1.91 million for the six months ended June 30, 2016 to \$1.43 million for the six months ended June 30, 2017. The decrease in revenue is attributable primarily to a decrease in advertising related bookings within our Rapid-Launch Games business, and it was partially offset by an increase in consumer app-store transaction bookings within our Full-Featured Games business.

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Revenue by Game Type			
Full-Featured	\$	295	\$ 135
Rapid-Launch		1,138	1,776
Total	\$	1,433	\$ 1,911

Our Full-Featured Games' revenue increased \$160 thousand, or 119%, from \$135 thousand for the six months ended June 30, 2016 to \$295 thousand for the six months ended June 30, 2017. The increase in Full-Featured revenue is attributable primarily to growth in player engagement and monetization within Video Poker Classic, and to the successful launches of Solitaire Dash and ROCKY™ between the comparable periods.

Our Rapid-Launch Games' revenue decreased \$638 thousand, or 36%, from \$1.78 million for the six months ended June 30, 2016 to \$1.1 million for the six months ended June 30, 2017. The decrease in revenue is attributable primarily to a decrease in advertising related bookings stemming from a decrease in DAUs and ABPU across our Rapid-Launch Games portfolio.

Cost of Revenue

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Platform Fees	\$	420	\$ 570
Licensing + Royalties		18	12
Hosting		5	5
Total	\$	443	\$ 587

Our cost of revenue decreased \$144 thousand, or 25%, from \$587 thousand in the Six Months Ended June 30, 2016 to \$443 thousand in the six months ended June 30, 2017. This decrease was primarily due to a corresponding decrease in revenue during the same periods.

Research and Development Expenses

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Research and development	\$	35	\$ 53
Percentage of revenue		2%	3%

Our research and development expenses decreased \$18 thousand, or 34%, from \$53 thousand in the six months ended June 30, 2016 to \$35 thousand in the six months ended June 30, 2017. The decrease in research and development costs was primarily due to a decrease in revenue share associated with some of our older games.

Marketing Expenses

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Marketing and public relations	\$	335	\$ 220
Percentage of revenue		23%	12%

Our marketing expenses increased \$115 thousand, or 52%, from \$220 thousand in the six months ended June 30, 2016 to \$335 thousand in the six months ended June 30, 2017. The increase in 2017 was primarily due to higher marketing expenditures related to continued marketing investments to support our Full-Featured Games, and primarily Video Poker Classic and Solitaire Dash.

General and Administrative Expenses

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
General and administrative	\$	678	\$ 618
Percentage of revenue		47%	32%

Our general and administrative expenses increased \$60 thousand, or 10%, from \$618 thousand in the six months ended June 30, 2016 to \$678 thousand in the six months ended June 30, 2017. The increase in general and administrative expenses was primarily due to an increase in personnel and related expenditures during the comparable periods.

Amortization of capitalized software development

		Six Months Ended June 30,	
		2017	2016
		(In thousands)	
Amortization of capitalized software development	\$	376	\$ 386
Percentage of revenue		26%	20%

Our amortization of capitalized software development decreased \$10 thousand or 3% from \$386 thousand in the six months ended June 30, 2016 to \$376 thousand in the six months ended June 30, 2017. The decrease in amortization of capitalized software development was attributable to a reduction in development expenditures relating to our Rapid-Launch Games in 2017.

Liquidity and Capital Resources

General

At June 30, 2017, we had cash and cash equivalents of \$200 thousand and working capital (current assets less current liabilities) of \$67 thousand. We currently expect that our cash and cash equivalents on hand, and our cash flows from operations will be sufficient to meet our anticipated cash requirements during the twelve months ending June 30, 2018. However, we are currently in the process of raising additional funds to improve our working capital. Future financing may include the issuance of equity or debt securities, obtaining credit facilities, or other financing mechanisms. Furthermore, if we issue additional equity or debt securities, existing holders of our securities may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of existing holders of our securities.

	Six Months Ended June 30,	
	2017	2016
	(In thousands)	
Cash flows (used in) provided by:		
Operating activities	\$ (21)	\$ 438
Investing activities	(473)	(531)
Financing activities	104	(560)
(Decrease) in cash and cash equivalents	\$ (390)	\$ (653)

Operating Activities

Our cash flow from operations varies significantly from quarter to quarter and from year to year, depending on our operating results and the timing of operating cash receipts and payments.

In the six months ended June 30, 2017, net cash used in operating activities was \$21 thousand, which was primarily due to a \$2.42 million net loss, a \$89 thousand increase in prepaid expenses, and a \$182 thousand decrease in accounts payable, accrued expenses and due to related parties. These amounts were offset by a \$74 thousand decrease in accounts receivable, a \$286 thousand increase in deferred revenue and adjustments for non-cash items, including stock-based compensation expense of \$62 thousand, amortization of software development costs of \$376 thousand, depreciation and amortization of other assets of \$12 thousand, amortization of debt discount of \$841 thousand, amortization of original issue discount of \$186 thousand and a loss on extinguishment of \$830 thousand.

In the six months ended June 30, 2016, net cash provided by operating activities was \$438 thousand, which was due to a net loss of \$810 thousand, a \$33 thousand decrease in prepaid expenses, a \$3 thousand decrease in accounts payable, accrued expenses and due to related parties. These amounts were offset by a \$70 thousand decrease in accounts receivable, and adjustments for non-cash items, amortization of software development costs of \$387 thousand, depreciation and amortization of other assets of \$39 thousand, amortization of debt discount of \$648 thousand, amortization of original issue discount of \$76 thousand.

Investing Activities

Cash used in investing activities in the six months ended June 30, 2017 was \$473 thousand, which was primarily due to \$469 thousand of capitalized software development costs related to the development of our mobile games and \$4 thousand of purchase of property, plant and equipment during the period.

Cash used in investing activities in the six months ended June 30, 2016 was \$531 thousand, which was primarily due to \$521 thousand of capitalized software development costs related to the development of our mobile games and \$10 thousand of purchase of property, plant and equipment during the period.

Financing Activities

Cash provided by financing activities in the six months ended June 30, 2017 was \$104 thousand, which was primarily due to \$350 thousand in proceeds received from the sales of common stock, offset by a \$234 thousand principal repayment of our Senior Convertible Debenture and \$13 thousand of financing costs incurred during the period.

Cash used by financing activities in the six months ended June 30, 2016 was \$560 thousand, which was due to a \$560 thousand principal repayment of our Senior Convertible Debenture.

Contractual Obligations and Other Commercial Commitments

Smaller reporting companies are not required to provide the information required by this item.

Off-Balance Sheet Arrangements

At June 30, 2017, we did not have any “off-balance sheet arrangements,” as defined in relevant SEC regulations that are reasonably likely to have a current or future effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources, other than the following.