



**TIX CORPORATION**

**ANNUAL REPORT**

**FOR THE FISCAL YEAR ENDED**

**DECEMBER 31, 2016**

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### Management's Discussion and Analysis of Financial Condition and Results of Operations

*The following discussion should be read in conjunction with the information contained in our consolidated financial statements, including the notes thereto. Statements regarding future economic performance, management's plans and objectives, and any statements concerning assumptions related to the foregoing contained in Management's Discussion and Analysis or Plan of Operation constitute forward-looking statements. Certain factors which may cause actual results to vary materially from these forward-looking statements accompany such statements or appears elsewhere in this Annual Report. Any references to "Tix" (which may be referred to as the "Company", "we", "us" or "our") means Tix Corporation and its subsidiary, as the context requires. You should read the following discussion of our financial condition and results of operations together with the consolidated financial statements and notes to the consolidated financial statements included elsewhere in this annual report.*

#### Forward-Looking Statements

Forward-looking statements include, but are not limited to, statements about our financial position, business strategy, competitive position, potential growth opportunities, potential operating performance improvements, and the effects of competition, the effects of future legislation or regulations and plans and objectives of our management for future operations. We have based our forward-looking statements on our management's beliefs and assumptions based on information available to our management at the time the statements are made. Use of the words "may," "should," "continue," "plan," "potential," "anticipate," "believe," "estimate," "expect," "intend," "outlook," "could," "project," "seek," "predict" or variations of such words and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties that could cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to, those set forth herein under Risk Factors, as well as other factors described herein or in our annual, quarterly and other reports we filed with the OTCQX (collectively, "Cautionary Statements"). Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described in any forward-looking statements. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the applicable Cautionary Statements. We do not intend to update these forward-looking statements, except as required by applicable law.

#### Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements is in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amount of revenues and expenses during the reporting period. Management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions.

The following narrative describes the critical accounting policies that affect the more significant judgments and estimates used in the preparation of the Company's consolidated financial statements.

#### Revenue Recognition and Presentation

The Company has several streams of revenue, each of which is required under Generally Accepted Accounting Principles ("GAAP") to be recognized in varying ways. The following is a summary of our revenue recognition policies:

The Company's Las Vegas discount show ticketing business recognizes as revenue the commissions and related transaction fees earned from the sale of Las Vegas show tickets at the time the tickets are paid for by and delivered to the customers. The Company's transaction fees are charged on a per-ticket basis. With certain exceptions, ticket sales are generally non-refundable, although same-day exchanges of previously sold tickets are permitted. Claims for ticket refunds, which are generally received and paid the day after the show date, are charged back to the respective shows and are recorded as a reduction to the Company's commissions and fees at the time that such refunds are processed. The Company does not have accounts receivable associated with its sales transactions, as payment is collected at the time of sale.

The Company's Las Vegas discounted dinners business offers reservations for discounted dinners at various restaurants surrounding the Las Vegas Strip and downtown with dining at specific times on the same day or in some cases the day after the sale. The

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Company recognizes as revenue the transaction fees earned from the booking of dinner reservations at the time that the reservations are made and a subsequent nominal fee from the restaurant at the time the reservation is used. At this time, the Company has immaterial amounts of accounts receivable and does not have any accounts payable associated with the discounted dinner business, as the Company collects the transaction fee at the time that the reservation is made, and the dinner payment is collected directly by the restaurant.

#### **Stock-Based Compensation**

Our stock-based employee compensation plans are described in Note 9 of the Notes to our Consolidated Financial Statements. The Company periodically issues stock options and warrants to employees. The Company accounts for stock option and warrant grants issued and vesting to employees based on the authoritative guidance provided by the ASC Topic 718 – *Stock Compensation* whereas the value of the award is measured on the date of grant and recognized over the vesting period.

The fair value of the Company's common stock option grant is estimated using the Black-Scholes option pricing model, which uses certain assumptions related to risk-free interest rates, expected volatility, expected life of the common stock options, and future dividends. Compensation expense is recorded based upon the value derived from the Black-Scholes option pricing model, and based on actual experience. The assumptions used in the Black-Scholes option pricing model could materially affect compensation expense recorded in future periods.

#### **Impairment of Long-Lived Assets, Goodwill and Intangible Assets**

We review long-lived assets whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable in accordance with the authoritative guidance provided by the ASC Topic 350 – *Goodwill and Other*. Our long-lived assets, such as property and equipment, are reviewed for impairment when events and circumstances indicate that depreciable or amortizable long lived assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of those assets. When specific assets are determined to be unrecoverable, the cost basis of the asset is reduced to reflect the current value.

We use various assumptions in determining the current fair value of these assets, including future expected cash flows and discount rates, as well as other fair value measurements. Our impairment loss calculations require us to apply judgment in estimating future cash flows, including forecasting useful lives of the assets and selecting the discount rate that reflects the risk inherent in future cash flows.

If actual results are not consistent with our assumptions and judgments used in estimating future cash flows and asset fair values, we may be exposed to future impairment losses that could be material to our results.

#### **Valuation of Intangible Assets**

The Company has acquired significant intangible assets that we recorded at fair value. The authoritative guidance provided by the ASC Topic 350 – *Goodwill and Other* requires us to make assumptions regarding inputs into the discounted cash flow model about the timing and amount of future net cash flows, risk, cost of capital, terminal values and market participants. Each of these factors can significantly affect the value of the intangible asset. The Company reviews intangible assets for impairment annually using an undiscounted net cash flows approach. If the undiscounted cash flows of an intangible asset are less than the carrying value of an intangible asset, the intangible asset is written down to its fair value, which is usually the discounted cash flow amount. Where cash flows cannot be identified for an individual asset, the review is applied at the lowest group level for which cash flows are identifiable. Goodwill and intangible assets are reviewed for impairment annually or when an event that could result in an impairment of goodwill occurs. At December 31, 2016, goodwill and intangibles amounted to \$3.1 million and amortization expense for intangible assets amounted to \$17,000 in 2016.

#### **Income Taxes**

The Company accounts for income taxes using the asset and liability method whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized before the Company is able to realize their benefits, or that future deductibility is uncertain. The Company considers future taxable income and ongoing, prudent and feasible tax planning strategies, in assessing the value of its deferred tax assets. During the year ended December 31, 2015, the Company recorded a deferred tax asset of \$11.5 million as it determined it was

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more likely than not that it would recover this asset against future earnings. If the Company determines that it is more likely than not that these assets will not be realized, the Company will reduce the value of these assets to their expected realizable value, thereby decreasing net income. Evaluating the value of these assets is necessarily based on the Company's judgment. If the Company subsequently determined that the deferred tax assets, which had been written down, would be realized in the future, the value of the deferred tax assets would be increased, thereby increasing net income in the period when that determination was made.

The Company prescribes a recognition threshold and a measurement attributable for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more likely than not to be sustained upon examination by taxing authorities. The amount recognized is measured as the largest amount of benefit that is greater than 50% likely of being realized.

The Company identified and reviewed potential tax uncertainties and determined that the exposure to those uncertainties did not have a material impact on the Company's results of operations or financial condition as of December 31, 2016 and 2015.

### **Recent Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*. ASU 2014-09 is a comprehensive revenue recognition standard that will supersede nearly all existing revenue recognition guidance under current U.S. GAAP and replace it with a principle based approach for determining revenue recognition. ASU 2014-09 will require that companies recognize revenue based on the value of transferred goods or services as they occur in the contract. The ASU also will require additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for interim and annual periods beginning after December 15, 2017. Early adoption is permitted only in annual reporting periods beginning after December 15, 2016, including interim periods therein. Entities will be able to transition to the standard either retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company is in the process of evaluating the impact of ASU 2014-09 on the Company's financial statements and disclosures but does not believe it will have a material effect.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. ASU 2016-02 requires a lessee to record a right of use asset and a corresponding lease liability on the balance sheet for all leases with terms longer than 12 months. ASU 2016-02 is effective for all interim and annual reporting periods beginning after December 15, 2018. Early adoption is permitted. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the expected impact that the standard could have on its financial statements and related disclosures.

In March 2016, the FASB issued the ASU 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. The amendments in this ASU require, among other things, that all income tax effects of awards be recognized in the income statement when the awards vest or are settled. The ASU also allows for an employer to repurchase more of an employee's shares than it can today for tax withholding purposes without triggering liability accounting and allows for a policy election to account for forfeitures as they occur. The amendments in this ASU are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted for any entity in any interim or annual period. The Company is currently evaluating the expected impact that the standard could have on its financial statements and related disclosures.

Other recent accounting pronouncements issued by the FASB, including its Emerging Issues Task Force, the American Institute of Certified Public Accountants, and the Securities and Exchange Commission did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

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## Results of Operations

### Consolidated Results of Operations

	Twelve Months Ended December 31,			% change 2016 v 2015	% change 2015 v 2014
	2016	2015	2014	2015	2014
Revenues	\$ 21,354,000	\$ 23,421,000	\$ 22,696,000	-9%	3%
Operating expenses:					
Direct operating expenses	10,147,000	9,395,000	9,441,000	8%	0%
Selling, general and administrative expenses	7,743,000	7,899,000	7,943,000	-2%	-1%
Depreciation and amortization	411,000	596,000	855,000	-31%	-30%
Total costs and expenses	18,301,000	17,890,000	18,239,000	2%	-2%
Operating income	3,053,000	5,531,000	4,457,000	-45%	24%
Operating margin	14%	24%	20%		
Other expense, net	22,000	15,000	209,000	47%	-93%
Income before provision for income tax expense (benefit)	3,031,000	5,516,000	4,248,000	-45%	30%
Provision for income tax expense (benefit)	1,128,000	(11,276,000)	100,000	-110%	11,376%
Net income	\$ 1,903,000	\$ 16,792,000	\$ 4,148,000	-89%	305%

## Revenues

The Company's Las Vegas discount show ticketing business recognizes as revenue the commissions and related transaction fees earned from the sale of Las Vegas show tickets at the time the tickets are paid for by and delivered to the customers. The Company's transaction fees are charged on a per-ticket basis. With certain exceptions, ticket sales are generally non-refundable, although same-day exchanges of previously sold tickets are permitted. Claims for ticket refunds, which are generally received and paid the day after the show date, are charged back to the respective shows and are recorded as a reduction to the Company's commissions and fees at the time that such refunds are processed. The Company does not have accounts receivable associated with its sales transactions, as payment is collected at the time of sale.

The Company offers reservations for discounted dinners at various restaurants surrounding the Las Vegas Strip and downtown. Revenues are recognized as transaction fees and are earned from the purchaser of the dinner reservations at the time the reservations are made and a subsequent nominal fee from the restaurant at the time the reservation is used. At this time, the Company has minor amounts of accounts receivable.

On May 5, 2016, the Company announced that Tix4Tonight had entered into an agreement with Expedia Local Expert, a division of Expedia, Inc., one of the world's largest online travel agencies (the "Expedia Agreement"). Under the terms of the Expedia Agreement, Tix4Tonight will serve as the Official Las Vegas Guest Services Partner for Expedia and its other brands. The service will provide both pre-arrival concierge-type services and in-market concierge-type desk services and related customer service support at physical locations in Las Vegas, featuring Tix4Tonight's inventory of discount show and attraction tickets, along with discount dining reservations. The project will also include some cross-sales efforts of online products. Tix4Tonight will operate all new co-branded locations and converted three of its existing locations to Expedia Local Expert. Tix4Tonight's remaining locations will continue to be operated separately. The Expedia Agreement was effective as of July 15, 2016. The Company anticipates generating revenue under the agreement in calendar year 2017.

Revenues were \$21.4 million and \$23.4 million for the years ended December 31, 2016 and 2015, respectively. Revenues were negatively impacted by decreased consumer demand for show tickets in the Las Vegas marketplace, the recent permanent closure of a Cirque du Soleil show for which we had significant sales in the prior year, and increased competition from online ticket brokers, show producers and hotel properties aggressively marketing to consumers. Our revenues were also negatively impacted

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by consumer demand for lower priced shows and attractions, which carried lower commissions and fees, as compared to the same period a year ago.

Revenues were \$23.4 million and \$22.7 million for the years ended December 31, 2015 and 2014, respectively.

### **Direct Operating Expenses**

Direct operating expenses include payroll costs, rents, utilities and third party commission and fees.

Direct operating expenses were \$10.1 million and \$9.4 million for the years ended December 31, 2016 and 2015, respectively. The increase in direct operating expenses was due to increased locations in operation, increased headcount and increased hourly payroll costs as compared to the same period a year ago. Direct operating expenses, as a percentage of revenues, were 48% and 40% for the years ended December 31, 2016 and 2015, respectively.

Direct operating expenses were \$9.4 million for both years ended December 31, 2015 and 2014, respectively. Direct operating expenses, as a percentage of revenues, were 40% and 42% for the years ended December 31, 2015 and 2014, respectively.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses include expenses that relate to activities directed by our executive offices including corporate personnel costs, insurance, litigation, legal and accounting fees, stock based compensation expense, consulting and advisory fees, regulatory compliance costs, board of directors' fees and corporate occupancy costs. In addition, selling, general and administrative expenses include merchant credit card processing fees, employee benefit expenses, advertising and miscellaneous other general operating expenses to support our business.

Selling, general and administrative expenses were \$7.8 million and \$7.9 million for the years ended December 31, 2016 and 2015, respectively. Selling, general and administrative expenses, as a percentage of revenues, were 36% and 34% for the years ended December 31, 2016 and 2015, respectively.

Selling, general and administrative expenses for both years ended December 31, 2015 and 2014 were \$7.9 million. Selling, general and administrative expenses, as a percentage of revenues, were 34% and 35% for the years ended December 31, 2015 and 2014, respectively.

### **Depreciation and Amortization**

Depreciation and amortization expense for the years ended December 31, 2016 and 2015 were \$411,000 and \$596,000, respectively. The decrease in depreciation and amortization expense was from property and equipment which became fully depreciated and intangible assets which became fully amortized during the same period of the prior year.

Depreciation and amortization expense for the years ended December 31, 2015 and 2014 were \$596,000 and \$855,000, respectively. The decrease in depreciation and amortization expense was from property and equipment which became fully depreciated and intangible assets which became fully amortized during the same period of the prior year.

### **Other Expense, Net**

Other expense, net for the years ended December 31, 2016 and 2015 were \$22,000 and \$15,000, respectively.

Other expense, net for the years ended December 31, 2015 and 2014 were \$15,000 and \$209,000, respectively. The decrease of \$194,000 was due primarily to decreased interest expense of \$190,000 associated with our debt balances.

### **Provision for Income Tax Expense (Benefit)**

Provision for income tax expense was \$1.1 million compared to a income tax benefit of \$11.3 million for the same period a year ago. During the year ended December 31, 2016, the company paid \$105,000 of federal income taxes relating to alternative minimum taxes. The difference between the \$1.0 million provision for income taxes and the \$105,000 paid in federal alternative minimum taxes was the change in our deferred tax asset during the year. For the year ended December 31, 2015, we recorded a benefit from income taxes of approximately \$11.3 million primarily related to reversing the valuation allowance against our

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deferred tax assets of \$11.5 million (see Note 11 to our Consolidated Financial Statements). The \$11.5 million income tax benefit was offset by \$254,000 of federal income taxes paid relating to alternative minimum tax.

## Adjusted EBITDA (Non-GAAP Financial Measure)

We use both GAAP and non-GAAP metrics to measure our financial results. We believe that, in addition to GAAP metrics, these non-GAAP metrics assist us in measuring our cash generated from operations. We believe this information is also useful to investors and other interested parties as our non-GAAP metrics removes non-cash and nonrecurring charges that occur in the affected period and provides a basis for measuring the Company's financial condition against historical results.

The Company defines Adjusted EBITDA as net income plus (a) other expense, net, (b) income taxes, (c) depreciation and amortization charges, (d) stock based compensation expense, (e) loss on disposition of property and equipment, (f) unusual litigation and (g) expenses for certain non-recurring matters requiring legal and advisory services relating to corporate and governance matters. Adjusted EBITDA does not represent net income or cash flows from operations as defined by GAAP; is not necessarily indicative of cash available to fund the Company's cash flow needs; and should not be considered as an alternative to net income, operating income, cash flows from operating activities or the Company's other financial information as determined under GAAP.

The following is a reconciliation of net income to Adjusted EBITDA for the years ended December 31, 2016, 2015 and 2014, respectively:

	Years Ended December 31,		
	2016	2015	2014
Net income	\$ 1,903,000	\$ 16,792,000	\$ 4,148,000
Income tax (benefit) expense	1,128,000	(11,276,000)	100,000
Other expense	22,000	15,000	209,000
Depreciation and amortization	411,000	596,000	855,000
Stock based compensation expense	404,000	366,000	429,000
Litigation expense and non-routine legal and advisory services for corporate and governance matters.	-	-	109,000
Adjusted EBITDA	\$ 3,868,000	\$ 6,493,000	\$ 5,850,000

## Off-Balance Sheet Arrangements

As of December 31, 2016, we did not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

## Liquidity and Capital Resources

### *Fiscal year ended December 31, 2016*

At December 31, 2016, we had cash of \$7.3 million and total assets of \$21.5 million compared to \$7.9 million and \$23.4 million at December 31, 2015. Our working capital decreased \$287,000 to \$5.1 million at December 31, 2016, compared to a working capital of \$5.4 million at December 31, 2015.

Cash flows provided from operating activities were \$3.4 million for the year ended December 31, 2016. Cash flows from operating activities were derived from our net income of \$1.9 million and increased by net non-cash charges, which include changes in the deferred tax asset, imputed interest, stock based compensation expense, depreciation, and intangible assets amortization. Total non-cash charges were \$1.9 million. The net income plus the non-cash charges were offset by changes in



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working capital accounts of \$347,000, which included a decrease in accounts payable and accrued expenses of \$343,000. The remaining change was due to small differences in several smaller working capital accounts.

Cash used in investing activities was \$80,000 for the year ended December 31, 2016 which was used to purchase property and equipment.

Cash used in financing activities was \$3.9 million for the year ended December 31, 2016, which includes payment of cash dividends of \$3.7 million (See Note 8 to our Consolidated Financial Statements), payment of \$200,000 on our note payable (See Note 5 to our Consolidated Financial Statements); \$39,000 used to purchase treasury shares (See Note 8 to our Consolidated Financial Statements), and receipt of \$42,000 on the exercise of stock options.

*Fiscal year ended December 31, 2015*

At December 31, 2015, we had cash of \$7.9 million and total assets of \$23.4 million compared to \$4.9 million and \$9.3 million at December 31, 2014. The increase in our assets was mainly due to recognition of a deferred tax asset of \$11.5 million at December 31, 2015. Our working capital increased \$2.7 million to \$5.4 million at December 31, 2015, compared to a working capital of \$2.6 million at December 31, 2014.

Cash flows provided from operating activities were \$6.6 million for the year ended December 31, 2015. Cash flows from operating activities were derived from our net income of \$16.8 million and decreased by net non-cash charges, which include changes in the deferred tax valuation allowance, imputed interest, stock based compensation expense, depreciation, and intangible assets amortization. Total non-cash charges were \$10.5 million. The net income less the non-cash charges were offset by changes in working capital accounts of \$316,000, which included an increase in accounts payable and accrued expenses of \$356,000. The remaining change was due to small differences in several smaller working capital accounts.

Cash used in investing activities was \$121,000 for the year ended December 31, 2015 which was used to purchase property and equipment.

Cash used in financing activities was \$3.4 million for the year ended December 31, 2015, which includes payment of cash dividends of \$2.6 million (See Note 8 to our Consolidated Financial Statements), payment of \$200,000 on our note payable (See Note 5 to our Consolidated Financial Statements); \$159,000 advanced to certain officers and employees to purchase shares of the Company's common stock (see Note 6 to our Consolidated Financial Statements); \$495,000 used to purchase treasury shares (See Note 8 to our Consolidated Financial Statements), and receipt of \$25,000 on the exercise of stock options.

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### **Risk Factors**

Investing in our securities involves a significant degree of risk. We are subject to various risks, some of which are described below, that may materially affect our business, financial condition, results of operations or cash flows. An investor should carefully consider the risks and uncertainties described below and the other information in this annual report and other filings or press releases of the Company before deciding to purchase or sell the Company's common stock. Additional risks and uncertainties may also materially and adversely affect our business, financial condition, results of operations or cash flows. If any of these risks or uncertainties actually occurs, our business, financial condition, operating results or cash flows could be materially harmed. In that case, the trading price of the common stock could decline and an investor could lose all or part of his or her investment.

**WE MAY BE ADVERSELY AFFECTED BY AN ECONOMIC DOWNTURN, WHICH COULD AFFECT CONSUMER AND CORPORATE SPENDING, AND THEREFORE SIGNIFICANTLY ADVERSELY IMPACT OUR OPERATING RESULTS.**

The prolonged economic downturn over the past few years and adverse conditions in the local, regional, national and global markets have negatively affected our operations, and may continue to negatively affect our operations in the future. Our business depends on discretionary consumer and corporate spending. Economic contraction, economic uncertainty or the perception by our customers of weak or weakening economic conditions may result in reductions in ticket sales and our ability to generate revenue. The risks associated with our businesses become more acute in periods of economic contraction, which may be accompanied by a decrease in our ticket sales. There is evidence that this has, and continues to, affect demand for our services, and a continued decline in economic activity could adversely affect demand thus reducing our revenue and earnings. A sustained decline in economic conditions could result in a further decline in attendance at or reduction in the number of live entertainment events, which would have an adverse effect on our revenue and operating income.

In addition, many factors related to discretionary consumer spending and corporate spending, including economic conditions affecting disposable consumer income such as employment, fuel prices, interest rates, tax rates, inflation and fears of war and future acts of terrorism can significantly impact our operating results.

**BECAUSE OUR BUSINESS OF SELLING DISCOUNT SHOW AND DISCOUNT DINNER RESERVATIONS IS CONCENTRATED IN LAS VEGAS, WE ARE SUBJECT TO GREATER RISKS THAN A COMPANY THAT IS MORE GEOGRAPHICALLY DIVERSIFIED.**

Our wholly-owned subsidiary, Tix4Tonight, offers for sale discount tickets to Las Vegas shows and discounted dinners reservations at various restaurants surrounding the Las Vegas Strip and downtown. Given that our ticket sales and dinner reservations are concentrated only in the Las Vegas area, our business may be significantly affected by risks common to the Las Vegas tourism industry. For example, the cost and availability of air services and the impact of any events that disrupt air travel to and from Las Vegas can adversely affect our business. We cannot control the number or frequency of flights to or from Las Vegas, but we rely on air traffic to deliver a significant portion of our customers. Reductions in flights by major airlines as a result of higher fuel prices or lower demand can impact the number of customers purchasing tickets to Las Vegas shows and dinner reservations at Las Vegas restaurants. Additionally, there is one principal interstate highway between Las Vegas and Southern California, where a large number of our customers reside. Capacity constraints of that highway or any other traffic disruptions may also affect the number of visitors to Las Vegas and therefore the customers who purchase tickets or dinner reservations. In addition, the growth of gaming in areas outside Las Vegas may result in a decrease of customer visits to Las Vegas and, in turn, a decrease in ticket sales.

**WE HAVE REVENUE CONCENTRATION THAT MAY IMPACT OUR FUTURE REVENUE GROWTH OR OTHERWISE AFFECT PROFITABILITY OF OUR BUSINESS**

During calendar years 2016 and 2015, Cirque du Soleil and MGM Resorts International were partners on six shows, which together represented approximately 14% and 18% of the number of show tickets we sold annually, respectively. If our existing relationships with MGM Resorts International or Cirque du Soleil materially deteriorate or are terminated and we are not successful in replacing lost business, our financial position, results of operations and cash flows could be materially and adversely affected. No single show, venue or theatre accounted for more than 10% of revenues.

**THERE IS A LIMITED PUBLIC MARKET FOR OUR COMMON STOCK AND THE COMPANY'S STOCKHOLDERS MAY BE UNABLE TO LIQUIDATE THEIR SHARES OR COULD BE SUBJECT TO EXTREME VOLATILITY.**

Our common stock is listed on the OTCQX marketplace and is quoted under the symbol "TIXC." There is currently a limited public market for our stock, thus providing limited liquidity into the market for the Company's shares, and there can be no assurance that an

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active trading market will develop or, if one does develop, that it will be maintained. As a result of the foregoing, stockholders may be unable to liquidate their shares or if a large volume of stock is being sold into the market at any one time, the price of our stock could rapidly decline.

### LOSS OF OUR KEY MANAGEMENT COULD NEGATIVELY IMPACT OUR BUSINESS.

The entertainment industry is uniquely dependent upon personal relationships. As executives within the entertainment industry, we leverage our existing network of relationships with producers, promoters, and venue managers in order to secure the rights to distribute tickets and secure the other resources that are critical to our success. Due to the importance of those industry contacts to our business, the loss of any of our officers, including Mitch Francis, our President and Chief Executive Officer, could adversely affect our operations. The death or disability of Mr. Francis or other extended or permanent loss of his services, or any negative market or industry perception with respect to him or arising from his loss, could have a material adverse effect on our business. Our other officers also have substantial experience and expertise in our business and the unexpected loss of services of one or more of these individuals could also adversely affect us. We have entered into employment agreements with our officers to protect our interests in those relationships, but we can give no assurance that all or any of our officers will remain with us or will retain their associations with key contacts.

### OUR OPERATIONS ARE SUBJECT TO INTENSE COMPETITION AND COMPETITIVE PRESSURES THAT COULD ADVERSELY AFFECT THE COMPANY'S BUSINESS, RESULTS OF OPERATIONS AND FINANCIAL CONDITION.

Tix4Tonight sells unsold tickets on the same day of the performance, generally at 25% to 50% off the box office price. Producers provide such tickets to the Company both on an exclusive and non-exclusive basis. Therefore, new ticket brokers can enter into competition with the Company to offer the same or similar ticketing services to non-exclusive shows and customers. Tix4Tonight faces competition from venues and producers selling discount tickets direct to customers, from online discount ticket sellers and the possibility exists for other competitors to compete both in Las Vegas and in other markets targeted by the Company. Other competitors may possess longer operating histories, larger customer bases, longer relationships with producers, and significantly greater financial, technical, marketing, and public relations resources than the Company. Accordingly, we may not be able to compete successfully and competitive pressures may adversely affect our business, results of operations and financial condition. We believe that barriers to entry into the business segments that we compete in are low and that certain local ticket brokers, promoters and producers are increasingly expanding the geographic scope of their operations.

### THE SUCCESS OF OUR BUSINESS DEPENDS IN PART ON THE INTEGRITY OF OUR SYSTEMS AND INFRASTRUCTURE. SYSTEM INTERRUPTION AND LACK OF INTEGRATION AND REDUNDANCY IN THESE SYSTEMS AND INFRASTRUCTURE MAY HAVE AN ADVERSE IMPACT ON OUR BUSINESS, FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The success of our business depends in part on our ability to maintain the integrity of our system and infrastructure, including websites, information and related systems, and distribution facilities. System interruption and the lack of integration and redundancy in the information systems and infrastructures of our ticketing operations may adversely affect our ability to process and fulfill transactions, respond to customer inquiries and generally maintain cost-efficient operations. We may experience occasional system interruptions that make some or all systems or data unavailable, or prevent us from efficiently providing services or fulfilling orders. We also rely on affiliate and third-party computer systems, broadband and other communications systems and service providers in connection with the provision of services generally, as well as to facilitate, process and fulfill transactions. Any interruptions, outages or delays in the systems and infrastructures of our business, our affiliates and/or third parties, or deterioration in the performance of these systems and infrastructures, could impair the ability of our business to provide services, fulfill orders and/or process transactions. Fire, flood, power loss, telecommunications failure, acts of war or terrorism, acts of God and similar events, or disruptions may damage or interrupt computer, broadband or other communications systems and infrastructures at any time. Any of these events could cause system interruption, delays and loss of critical data, and could prevent us from providing services, fulfilling orders and/or processing transactions. While we have backup systems for certain aspects of our operations, these systems are not fully redundant and disaster recovery planning is not sufficient for all eventualities. In addition, we may not have adequate insurance coverage to compensate for losses from a major interruption. If any of these adverse events were to occur, it could adversely affect our business, financial condition and results of operations.

### THE PROCESSING, STORAGE, USE, AND DISCLOSURE OF PERSONAL DATA COULD GIVE RISE TO LIABILITIES AS A RESULT OF GOVERNMENTAL REGULATION, CONFLICTING LEGAL REQUIREMENTS OR DIFFERING VIEWS OF PERSONAL PRIVACY.

## TIX CORPORATION 2016 ANNUAL REPORT

In the processing of consumer transactions, we receive, transmit and store a large volume of personally identifiable information and other user data. The sharing, use, disclosure and protection of this information are governed by the respective privacy and data security policies maintained by our business. Moreover, there are federal, state and international laws regarding privacy and the storing, sharing, use, disclosure and protection of personally identifiable information and user data. Specifically, personally identifiable information is increasingly subject to legislation and regulations in numerous jurisdictions around the world, the intent of which is to protect the privacy of personal information that is collected, processed and transmitted in or from the governing jurisdiction. We could be adversely affected if legislation or regulations are expanded to require changes in business practices or privacy policies, or if governing jurisdictions interpret or implement their legislation or regulations in ways that negatively affect our business, financial condition and results of operations.

The failure by us and/or the various third-party vendors and service providers with which we do business, to comply with applicable privacy policies or federal, state or similar international laws and regulations, or any compromise of security that results in the unauthorized release of personally identifiable information or other user data could damage the reputation of our business, discourage potential users from trying the products and services that we offer, and/or result in fines and/or proceedings by governmental agencies and/or consumers, one or all of which could adversely affect our business, financial condition and results of operations.

**OUR EXISTING DIRECTORS, EXECUTIVE OFFICERS AND PRINCIPAL STOCKHOLDERS HOLD A SUBSTANTIAL AMOUNT OF THE COMPANY'S COMMON STOCK AND MAY BE ABLE TO PREVENT OTHER STOCKHOLDERS FROM INFLUENCING SIGNIFICANT CORPORATE DECISIONS.**

Based on information known to us as of December 31, 2016, our directors and executive officers and principal stockholders beneficially owned or have the right to vote approximately 64.6% of our outstanding common stock. Because beneficial owners are not required to disclose their ownership interests publicly or to the Company, we may only rely on public sources and reports made directly to us when determining beneficial ownership, and, as a result, there may be other beneficial owner(s) of more than 5% of the Company's Common Stock. Approximately 18.1% of our common stock is beneficially owned by Mitch Francis, our President and Chief Executive Officer, approximately 7.5% of our common stock is beneficially owned by our other officers and directors (other than Mr. Francis), approximately 15.9% of our common stock is beneficially owned by Bandera Master Fund LP, approximately 14.2% of our common stock is beneficially owned by Boston Avenue Capital LLC and approximately 8.8% of our common stock is beneficially owned by a private group of individual investors. These stockholders will be able to individually influence, or if acting in a similar manner, direct the outcome of matters, including the election of our directors and other corporate actions, such as a merger with or into another company, a sale of substantially all of the Company's assets, and amendments to the Company's Certificate of Incorporation. The decisions of these stockholders may conflict with the Company's interests or the interest of the Company's other stockholders.

**OUR BY-LAWS AND CERTIFICATE OF INCORPORATION CONTAIN PROVISIONS THAT MAY DISCOURAGE OR PREVENT A TAKEOVER OF OUR COMPANY.**

Provisions contained in the Company's by-laws, such as provisions requiring advance notice relating to certain stockholder business and Board of Directors nominees to be considered at stockholder meetings and provisions not permitting stockholders to call special meetings of stockholders, as well as provisions of the Delaware General Corporation Law, could delay or make it more difficult to remove incumbent directors or for a third party to acquire us. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace or remove our directors.

**ANTI-TAKEOVER EFFECTS OF OUR RIGHTS AGREEMENT MAY DELAY OR PREVENT A CHANGE OF CONTROL AND MAY ALSO MAKE A MERGER OR ACQUISITION OF THE COMPANY LESS DESIRABLE.**

The Board of Directors has adopted a Rights Agreement as of April 1, 2011, as amended and restated on January 2, 2014 ("Rights Agreement"), commonly known as a poison pill, which may delay or prevent a change of control and may also make a merger or acquisition of the Company less desirable. The Rights Agreement is generally triggered when an "Acquiring Person" (as defined by the Rights Agreement) acquires beneficial ownership of 4.95% or more of the common stock, with certain limited exceptions. Persons or groups who held 4.95% or more of the common stock as of January 2, 2014 are grandfathered under the Rights Agreement, meaning that they are not deemed to be Acquiring Persons unless and until they become the beneficial owner of any additional shares of common stock or they are grouped together with other stockholders for purposes of triggering the rights. The preceding description of the Amended and Restated Rights Agreement is qualified in its entirety by reference to the terms of the Amended and Restated Rights Agreement, a copy of which is available at [http://www.irdirect.net/TIXC/corporate\\_document/71](http://www.irdirect.net/TIXC/corporate_document/71).

## TIX CORPORATION 2016 ANNUAL REPORT

IF ECONOMIC CONDITIONS WORSEN CAUSING REDUCED EARNINGS, WE MAY INCUR GOODWILL AND INTANGIBLE ASSET IMPAIRMENTS THAT COULD NEGATIVELY AFFECT OUR FUTURE PROFITS.

As of December 31, 2016, we have remaining goodwill and intangible assets related to our acquisitions of \$3.1 million. In accordance with the authoritative guidance for goodwill and other intangible assets, we test our goodwill and intangible assets for impairment annually or if a triggering event occurs or when an event that could result in an impairment of goodwill occurs. Factors we consider important that could trigger an impairment review include significant underperformance relative to historical or projected future operating results, significant changes in the manner of the use of our assets or the strategy for our overall business, and significant negative industry or economic trends. If current economic conditions worsen causing decreased revenues and increased costs, we may have to recognize goodwill and intangible asset impairments, which could have a material adverse impact on our results of operations.

CERTAIN STOCK OWNERSHIP CHANGES COULD LIMIT THE FUTURE AVAILABILITY TO US OF ACCUMULATED NET OPERATING LOSS CARRY FORWARDS

At December 31, 2016, the Company estimates it had federal net operating loss carry forwards ("NOLs") of approximately \$25.7 million, which are subject to certain limitations, which begin expiring in 2017 in varying amounts through 2032. NOLs may be carried forward to offset taxable income in future years and eliminate income taxes otherwise payable on such taxable income, subject to certain adjustments. Based on current corporate income tax rates, our NOLs could provide a benefit to us, if fully utilized, of significant future tax savings. However, the Company's ability to use the federal NOLs would be substantially limited if there were an "ownership change" as defined under Section 382 of the U.S. Internal Revenue Code and related U.S. Treasury regulations. In general, an ownership change would occur if the Company's "5-percent shareholders," as defined under Section 382, collectively increase their ownership in the Company by more than 50 percentage points over a rolling three-year period. As discussed in the Company's press release, dated January 2, 2014, the Board of Directors has adopted an amendment of the Company's Rights Agreement that is intended to reduce the likelihood that changes in the Company's stockholder base have the unintended effect of limiting the Company's use of its NOLs. The Rights Agreement is generally triggered when an "Acquiring Person" (as defined by the Rights Agreement) acquires beneficial ownership of 4.95% or more of the common stock, with certain limited exceptions. Persons or groups who held 4.95% or more of the common stock as of January 2, 2014 are grandfathered under the Rights Agreement, meaning that they are not deemed to be Acquiring Persons unless and until they become the beneficial owner of any additional shares of common stock or they are grouped together with other stockholders for purposes of triggering the rights. This would protect the NOLs because changes in ownership by a person owning less than 4.95% of the Company's stock are not included in the calculation of "ownership change" for purposes of Section 382 of the Code. However, there can be no assurance that the Rights Agreement would be effective under all circumstances.

## INDEPENDENT AUDITOR'S REPORT

The Board of Directors  
Tix Corporation  
Studio City, California

### *Report on the Financial Statements*

We have audited the accompanying consolidated financial statements of Tix Corporation and subsidiary (the "Company"), which comprise the consolidated balance sheets as of December 31, 2016 and 2015 and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

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

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Tix Corporation and subsidiary as of December 31, 2016 and 2015, and the results of their consolidated operations and their cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

**Weinberg & Company, P.A.**  
Los Angeles, California  
February 21, 2016

**TIX CORPORATION AND SUBSIDIARY  
CONSOLIDATED BALANCE SHEETS**

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
<b>Assets</b>		
<b>Current assets:</b>		
Cash	\$ 7,336,000	\$ 7,921,000
Accounts receivable	36,000	47,000
Prepaid expenses and other current assets	131,000	122,000
<b>Total current assets</b>	<u>7,503,000</u>	<u>8,090,000</u>
<b>Property and equipment, net</b>	<u>264,000</u>	<u>579,000</u>
<b>Other assets:</b>		
Intangible assets:		
Goodwill	3,120,000	3,120,000
Intangibles, net	-	17,000
Total intangible assets	3,120,000	3,137,000
Deferred tax asset	10,508,000	11,531,000
Deposits and other assets	61,000	66,000
<b>Total other assets</b>	<u>13,689,000</u>	<u>14,734,000</u>
<b>Total assets</b>	<u>\$ 21,456,000</u>	<u>\$ 23,403,000</u>
<b>Liabilities and Stockholders' Equity</b>		
<b>Current liabilities:</b>		
Accounts payable – shows and events	\$ 1,097,000	\$ 1,140,000
Accounts payable and accrued expenses	1,090,000	1,390,000
Deferred revenue	44,000	25,000
Notes payable – short term and net of discount	200,000	176,000
<b>Total current liabilities</b>	<u>2,431,000</u>	<u>2,731,000</u>
Deferred rent obligations	28,000	58,000
Note payable – net of current portion and discount	176,000	376,000
<b>Total liabilities</b>	<u>2,635,000</u>	<u>3,165,000</u>
<b>Commitments and contingencies</b>		
<b>Stockholders' equity:</b>		
Preferred stock, \$.01 par value; 500,000 shares authorized; none issued		
Common stock, \$.08 par value; 100,000,000 shares authorized; 17,349,583 shares net of 16,637,406 treasury shares, and 17,280,009 shares net of 16,619,953 treasury shares issued and outstanding at December 31, 2016 and December 31, 2015, respectively	2,720,000	2,713,000
Additional paid-in capital	94,655,000	94,216,000
Cost of shares held in treasury	(28,154,000)	(28,115,000)
Accumulated deficit	(50,400,000)	(48,576,000)
<b>Total stockholders' equity</b>	<u>18,821,000</u>	<u>20,238,000</u>
<b>Total liabilities and stockholders' equity</b>	<u>\$ 21,456,000</u>	<u>\$ 23,403,000</u>

See accompanying notes to the consolidated financial statements.

**TIX CORPORATION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**YEARS ENDED DECEMBER 31, 2016 AND 2015**

	<b>Years Ended December 31,</b>	
	<b>2016</b>	<b>2015</b>
Revenues	\$ 21,354,000	\$ 23,421,000
Operating expenses:		
Direct costs of revenues	10,147,000	9,395,000
Selling, general and administrative expenses	7,743,000	7,899,000
Depreciation and amortization	411,000	596,000
Total costs and expenses	18,301,000	17,890,000
Operating income	3,053,000	5,531,000
Other (income) expense:		
Other income	-	(7,000)
Interest income	(2,000)	(2,000)
Interest expense	24,000	24,000
Other expense, net	22,000	15,000
Income before provision for income tax expense (benefit)	3,031,000	5,516,000
Provision for income tax expense (benefit)	1,128,000	(11,276,000)
Net income	\$ 1,903,000	\$ 16,792,000
Net income per common share		
Net income per common share – basic	\$ 0.11	\$ 0.98
Net income per common share – diluted	\$ 0.11	\$ 0.95
Weighted average common shares outstanding – basic	17,333,209	17,199,747
Weighted average common shares outstanding – diluted	18,097,102	17,741,834

See accompanying notes to the consolidated financial statements.



**TIX CORPORATION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**YEARS ENDED DECEMBER 31, 2016 AND 2015**

	Common stock		Additional	Obligation	Accumulated	Treasury	Total
	Shares	Amount	Paid In Capital	For Share Purchases	Deficit	Stock	Stockholders' Equity
Balance, December 31, 2014	17,864,744	\$ 2,666,000	\$ 93,865,000	\$ (2,148,000)	\$ (62,810,000)	\$ (25,465,000)	\$ 6,108,000
Cash dividends					(2,558,000)		(2,558,000)
Fair value of options and warrants issued to employees and directors	-	-	366,000	-	-	-	366,000
Shares issued on exercise of stock options on a cash basis	19,444	2,000	23,000	-	-	-	25,000
Shares issued on exercise of stock options on a cashless basis	563,971	45,000	(45,000)	-	-	-	-
Cost of treasury shares	(225,560)	-	-	-	-	(495,000)	(495,000)
Reclassify obligation for share purchase to treasury stock	(942,590)	-	7,000	2,148,000	-	(2,155,000)	-
Net Income	-	-	-	-	16,792,000	-	16,792,000
Balance, December 31, 2015	17,280,009	2,713,000	94,216,000	-	(48,576,000)	(28,115,000)	20,238,000
Cash dividends					(3,727,000)		(3,727,000)
Fair value of options and warrants issued to employees and directors	-	-	404,000	-	-	-	404,000
Shares issued on exercise of stock options on a cash basis	33,334	3,000	39,000	-	-	-	42,000
Shares issued on exercise of stock options on a cashless basis	53,693	4,000	(4,000)	-	-	-	-
Cost of treasury shares	(17,453)	-	-	-	-	(39,000)	(39,000)
Net Income	-	-	-	-	1,903,000	-	1,903,000
Balance, December 31, 2016	<u>17,349,583</u>	<u>\$ 2,720,000</u>	<u>\$ 94,655,000</u>	<u>\$ -</u>	<u>\$ (50,400,000)</u>	<u>\$ (28,154,000)</u>	<u>\$ 18,821,000</u>

See accompanying notes to the consolidated financial statements.

**TIX CORPORATION AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31, 2016 AND 2015**

	<b>Years Ended December 31,</b>	
	<b>2016</b>	<b>2015</b>
Cash flows from operating activities:		
Net income	\$ 1,903,000	\$ 16,792,000
<b>Adjustments to reconcile net income to cash provided by operating activities</b>		
Depreciation	395,000	460,000
Non-cash interest	24,000	24,000
Amortization of intangible assets	17,000	136,000
Change in deferred tax assets valuation allowance	1,023,000	(11,531,000)
Fair value of options and warrants issued to employees and directors	404,000	366,000
(Increase) decrease in:		
Accounts receivable	11,000	7,000
Prepaid expenses and other assets	(4,000)	28,000
Increase (decrease) in:		
Accounts payable – shows and events	(43,000)	202,000
Accounts payable and accrued expenses	(300,000)	154,000
Deferred revenue	19,000	-
Deferred rent obligation	(30,000)	(75,000)
Net cash provided by operating activities	<u>3,419,000</u>	<u>6,563,000</u>
Cash flows from investing activities:		
Purchases of property and equipment	<u>(80,000)</u>	<u>(121,000)</u>
Net cash used in investing activities	<u>(80,000)</u>	<u>(121,000)</u>
Cash flows from financing activities:		
Proceeds from exercise of stock options	42,000	25,000
Dividends paid	(3,727,000)	(2,558,000)
Cost of treasury stock, net of fees	(39,000)	(495,000)
Payment of notes payable	(200,000)	(200,000)
Obligation for shares purchases	<u>-</u>	<u>(159,000)</u>
Net cash used in financing activities	(3,924,000)	(3,387,000)
Net (decrease) increase	(585,000)	3,055,000
Balance at beginning of period	<u>7,921,000</u>	<u>4,866,000</u>
Balance at end of period	<u>\$ 7,336,000</u>	<u>\$ 7,921,000</u>
Supplemental disclosures of cash flow information:		
Cash paid for:		
Income taxes	\$ <u>120,000</u>	\$ <u>254,000</u>
Interest	\$ <u>-</u>	\$ <u>-</u>
<b>Non-cash financing activities:</b>		
Return of common stock to treasury	<u>\$ -</u>	<u>\$ 2,155,000</u>

See accompanying notes to the consolidated financial statements.

**TIX CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**YEARS ENDED DECEMBER 31, 2016 AND 2015**

**1. Organization and Basis of Presentation**

Tix Corporation (the “Company”) was incorporated in Delaware on April 6, 1993. The Company is an entertainment company providing discount ticketing and discount dinner reservations through our subsidiary Tix4Tonight, LLC (“Tix4Tonight”).

Our wholly-owned subsidiary, Tix4Tonight, offers for sale discount show and discount dinner reservations. When selling last minute discounted tickets, Tix4Tonight sells them under short-term, exclusive and nonexclusive agreements with nearly every Las Vegas show and numerous attractions and tours running at any one time. Tix4Tonight typically does not know exactly what shows it will be able to offer tickets for until the same day of the show. There are usually many more tickets available each day than are sold, although it is not uncommon for Tix4Tonight to sell out its supply of tickets for individual shows. The shows are paid on a weekly basis only for the tickets that Tix4Tonight actually sells to customers. Tix4Tonight has no financial risk with respect to unsold tickets and revenues are recorded at net of cost, that is, we record only the commissions and service fees as revenues.

On May 5, 2016, the Company announced that Tix4Tonight had entered into an agreement with Expedia Local Expert, a division of Expedia, Inc., one of the world’s largest online travel agencies (the “Expedia Agreement”). Under the terms of the Expedia Agreement, Tix4Tonight will serve as the Official Las Vegas Guest Services Partner for Expedia and its other brands. The service will provide both pre-arrival concierge-type services and in-market concierge-type desk services and related customer service support at physical locations in Las Vegas, featuring Tix4Tonight’s inventory of discount show and attraction tickets, along with discount dining reservations. The project will also include some cross-sales efforts of online products. Tix4Tonight will operate all new co-branded locations and converted three of its existing locations to Expedia Local Expert. Tix4Tonight’s remaining locations will continue to be operated separately. The Expedia Agreement was effective as of July 15, 2016.

**2. Summary of Significant Accounting Policies**

**Revenue Recognition**

The Company currently has two streams of revenue, each of which is required under Generally Accepted Accounting Principles (“GAAP”) to be recognized in varying ways. The following is a summary of our revenue recognition policies:

The Company’s Las Vegas discount show ticketing business recognizes as revenue the commissions and related transaction fees earned from the sale of Las Vegas show tickets at the time the tickets are paid for by and delivered to the customers. The Company’s transaction fees are charged on a per-ticket basis. With certain exceptions, ticket sales are generally non-refundable, although same-day exchanges of previously sold tickets are permitted. Claims for ticket refunds, which are generally received and paid the day after the show date, are charged back to the respective shows and are recorded as a reduction to the Company’s commissions and fees at the time that such refunds are processed. The Company does not have accounts receivable associated with its sales transactions, as payment is collected at the time of sale.

The Company’s Las Vegas discounted dinners business offers reservations for discounted dinners at various restaurants surrounding the Las Vegas Strip and downtown with dining at specific times on the same day or in some cases the day after the sale. The Company recognizes as revenue the transaction fees earned from the booking of dinner reservations at the time that the reservations are made and a subsequent nominal fee from the restaurant at the time the reservation is used. At this time, the Company has immaterial amounts of accounts receivable and does not have any accounts payable associated with the discounted dinner business, as the Company collects the transaction fee at the time that the reservation is made, and the dinner payment is collected directly by the restaurant.

**Revenue Concentrations**

During calendar years 2016 and 2015, Cirque du Soleil and MGM Resorts International were partners on six shows, which together represented approximately 14% and 18% of the number of show tickets we sold annually, respectively. If our existing relationships with MGM Resorts International or Cirque du Soleil materially deteriorate or are terminated and we are not successful in replacing lost business, our financial position, results of operations and cash flows could be materially and adversely affected. No single show, venue or theatre accounted for more than 10% of revenues.

**Consolidation**

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. Intercompany transactions and balances are eliminated in consolidation.

**TIX CORPORATION AND SUBSIDIARY**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**YEARS ENDED DECEMBER 31, 2016 AND 2015**

**Property and Equipment**

Property and equipment are stated at cost less accumulated depreciation or amortization. Depreciation is recorded at the time property and equipment is placed in service using the straight-line method over the estimated useful lives of the related assets, which range from one to ten years. Leasehold improvements are amortized over the shorter of the expected useful lives of the related assets or the lease term.

**Stock-Based Compensation**

The Company periodically issues stock options and warrants to employees. The Company accounts for stock option and warrant grants issued and vesting to employees based on the authoritative guidance provided by the ASC Topic 718 – *Stock Compensation* whereas the value of the award is measured on the date of grant and recognized over the vesting period.

The fair value of the Company's common stock option grants are estimated using the Black-Scholes option pricing model, which uses certain assumptions related to risk-free interest rates, expected volatility, expected life of the common stock options, and future dividends. Compensation expense is recorded based upon the value derived from the Black-Scholes option pricing model, and based on actual experience. The assumptions used in the Black-Scholes option pricing model could materially affect compensation expense recorded in future periods.

**Intangible Assets and Goodwill**

The Company accounts for intangible assets and goodwill in accordance with the authoritative guidance issued by the ASC Topic 350 – *Goodwill and Other*. Intangibles are valued at their fair market value and are amortized taking into account the character of the acquired intangible asset and the expected period of benefit. The Company evaluates intangible assets and goodwill for impairment, at a minimum, on an annual basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable from its estimated undiscounted future cash flows. Recoverability of goodwill and intangible assets is measured by comparing their net book value to the related projected undiscounted cash flows from these assets, considering a number of factors, including past operating results, budgets, economic projections, market trends and product development cycles. If the net book value of the asset exceeds the related undiscounted cash flows, the asset is considered impaired, and a second test is performed to measure the amount of impairment loss.

At December 31, 2016, the Company had remaining goodwill related to our acquisitions of \$3.1 million. There were no indications of impairment based on management's assessment of this asset at December 31, 2016. Factors we consider important that could trigger an impairment review include significant underperformance relative to historical or projected future operating results, significant changes in the manner of the use of our assets or the strategy for our overall business, and significant negative industry or economic trends. If current economic conditions worsen causing decreased revenues and increased costs, we may have to record an impairment to our goodwill.

**Income Taxes**

The Company accounts for income taxes using the asset and liability method whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized before the Company is able to realize their benefits, or that future deductibility is uncertain.

The Company considers future taxable income and ongoing, prudent and feasible tax planning strategies, in assessing the value of its deferred tax assets. During the year ended December 31, 2015, the Company recorded a deferred tax asset of \$11.5 million as it determined it was more likely than not that it would recover this asset against future earnings. If the Company determines that it is more likely than not that these assets will not be realized, the Company will reduce the value of these assets to their expected realizable value, thereby decreasing net income. Evaluating the value of these assets is necessarily based on the Company's judgment. If the Company subsequently determined that the deferred tax assets, which had been written down, would be realized in the future, the value of the deferred tax assets would be increased, thereby increasing net income in the period when that determination was made.

The Company prescribes a recognition threshold and a measurement attributable for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more likely than not to be sustained upon examination by taxing authorities. The amount recognized is measured as the largest amount of benefit that is greater than 50% likely of being realized.

**TIX CORPORATION AND SUBSIDIARY**  
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The Company identified and reviewed potential tax uncertainties and determined that the exposure to those uncertainties did not have a material impact on the Company's results of operations or financial condition as of December 31, 2016 and 2015.

**Deferred Rent Obligations**

Certain of the real estate operating lease agreements to which we are party contain rent escalation clauses or lease incentives, such as rent abatements or tenant improvement allowances. Rent escalation clauses and lease incentives are taken into account in determining total rent expense to be recognized during the term of the lease, which begins on the date that we take control of the leased space. Renewal options are considered when evaluating the overall term of the lease. In accordance with ASC Topic 840 – *Leases*, differences between periodic rent expense and periodic cash rental payments, caused primarily by the recognition of rent expense on a straight-line basis and tenant improvement allowances due or received from lessors, are recorded as deferred rent obligations on our consolidated balance sheets.

We record tenant improvement allowances as a deferred rent obligation on our consolidated balance sheets and as a cash inflow from operating activities in our consolidated statements of cash flows. We record capital expenditures funded by tenant improvement allowances received as a leasehold improvement on our consolidated balance sheets and as a capital expenditure within our consolidated statements of cash flows.

**Fair Value Measurements**

The Company uses various inputs in determining the fair value of its investments and measures these assets on a recurring basis. Financial assets recorded at fair value in the consolidated balance sheets are categorized by the level of objectivity associated with the inputs used to measure their fair value. Authoritative guidance provided by the ASC Topic 820 - *Fair Value Measurements and Disclosure* defines the following levels directly related to the amount of subjectivity associated with the inputs to fair valuation of these financial assets:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
- Level 2—Inputs, other than the quoted prices in active markets, that is observable either directly or indirectly.
- Level 3—Unobservable inputs based on the Company's assumptions.

The Company is required to use observable market data if such data is available without undue cost and effort. At December 31, 2016 and 2015, the fair value of cash, accounts receivable, prepaid expense and accounts payable approximate their fair values due to their short term nature. Notes payable approximates their fair value based on their effective interest rates.

**Basic and Diluted Income per Share**

Our computation of earnings per share ("EPS") includes basic and diluted EPS. Basic EPS is measured as the income available to common stockholders divided by the weighted average common shares outstanding for the period. Diluted income per share reflects the potential dilution, using the treasury stock method, that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the income of the Company as if they had been converted at the beginning of the periods presented, or issuance date, if later. In computing diluted income per share, the treasury stock method assumes that outstanding options and warrants are exercised and the proceeds are used to purchase common stock at the average market price during the period. Options and warrants may have a dilutive effect under the treasury stock method only when the average market price of the common stock during the period exceeds the exercise price of the options and warrants. Potential common shares that have an anti-dilutive effect (i.e., those that increase income per share or decrease loss per share) are excluded from the calculation of diluted EPS.

The following table sets forth the computation of basic and diluted income per common share.

	<b>Twelve Months Ended December 31,</b>	
	<b>2016</b>	<b>2015</b>
Net income	\$ 1,903,000	\$ 16,792,000
Weighted average common shares – basic	17,333,209	17,199,747
Dilutive effect of outstanding warrants and stock options	763,893	542,087

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Weighted average shares – diluted	18,097,102	17,741,834
Net income per common share:		
Basic	\$ 0.11	\$ 0.98
Diluted	\$ 0.11	\$ 0.94

There were no adjustments to net income required for purposes of computing diluted earnings per share. At December 31, 2016 and 2015, we excluded the outstanding securities summarized below, which entitle the holders thereof to acquire shares of common stock, from our calculation of our diluted earnings per share, as their effect would have been antidilutive.

	<b>December 31, 2016</b>	<b>December 31, 2015</b>
Stock Options	505,000	333,000

### Accounting 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include assumptions made in evaluating the realization of our deferred tax assets, the impairment analysis of goodwill and intangible assets, potential liabilities and the assumptions made in valuing stock instruments issued for services.

### Advertising Costs

Advertising costs are charged to operations as part of selling, general and administrative expenses at the time the costs are incurred. Advertising costs for the years ended December 31, 2016 and 2015 were \$458,000 and \$420,000, respectively.

### Concentration of Credit Risk

The Company maintains the majority of its cash balances with one financial institution, in the form of demand deposits. At December 31, 2016 and 2015, the Company had cash deposits that exceeded the federally insured limit of \$250,000. The Company believes that no significant concentration of credit risk exists with respect to these cash balances because of its assessment of the creditworthiness and financial viability of the financial institution.

### Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*. ASU 2014-09 is a comprehensive revenue recognition standard that will supersede nearly all existing revenue recognition guidance under current U.S. GAAP and replace it with a principle based approach for determining revenue recognition. ASU 2014-09 will require that companies recognize revenue based on the value of transferred goods or services as they occur in the contract. The ASU also will require additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for interim and annual periods beginning after December 15, 2017. Early adoption is permitted only in annual reporting periods beginning after December 15, 2016, including interim periods therein. Entities will be able to transition to the standard either retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company is in the process of evaluating the impact of ASU 2014-09 on the Company's financial statements and disclosures but does not believe it will have a material effect.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. ASU 2016-02 requires a lessee to record a right of use asset and a corresponding lease liability on the balance sheet for all leases with terms longer than 12 months. ASU 2016-02 is effective for all interim and annual reporting periods beginning after December 15, 2018. Early adoption is permitted. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The

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Company is currently evaluating the expected impact that the standard could have on its financial statements and related disclosures.

In March 2016, the FASB issued the ASU 2016-09, *Compensation - Stock Compensation (Topic 718)*: Improvements to Employee Share-Based Payment Accounting. The amendments in this ASU require, among other things, that all income tax effects of awards be recognized in the income statement when the awards vest or are settled. The ASU also allows for an employer to repurchase more of an employee's shares than it can today for tax withholding purposes without triggering liability accounting and allows for a policy election to account for forfeitures as they occur. The amendments in this ASU are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted for any entity in any interim or annual period. The Company is currently evaluating the expected impact that the standard could have on its financial statements and related disclosures.

Other recent accounting pronouncements issued by the FASB, including its Emerging Issues Task Force, the American Institute of Certified Public Accountants, and the Securities and Exchange Commission did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

### 3. Property and Equipment

The table below displays our property and equipment balances as of December 31, 2016 and 2015, respectively.

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Office equipment and furniture	\$ 3,505,000	\$ 3,425,000
Leasehold improvements	<u>287,000</u>	<u>287,000</u>
Total property and equipment	3,792,000	3,712,000
Less accumulated depreciation	<u>(3,528,000)</u>	<u>(3,133,000)</u>
Total property and equipment, net	<u>\$ 264,000</u>	<u>\$ 579,000</u>

Depreciation expense was \$394,000 and \$460,000 for the years ended December 31, 2016 and 2015, respectively.

### 4. Goodwill and Intangible Assets

The following table summarizes the original cost of goodwill and intangible assets, net of related accumulated amortization, at December 31, 2016 and 2015, respectively:

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Contract commitments	\$ 2,242,000	\$ 2,242,000
Intellectual property (e.g. domain names)	<u>130,000</u>	<u>130,000</u>
Total intangible assets	2,372,000	2,372,000
Less accumulated amortization	<u>(2,372,000)</u>	<u>(2,355,000)</u>
Total intangible assets, net	-	17,000
Goodwill	<u>3,120,000</u>	<u>3,120,000</u>
Total goodwill and intangible assets, net	<u>\$ 3,120,000</u>	<u>\$ 3,137,000</u>

Amortization expense related to intangible assets in 2016 and 2015 was \$17,000 and \$136,000, respectively.

### 5. Note Payable

On February 10, 2011, the Company entered into and concurrently closed on an Asset Purchase Agreement with VegasTix4Less. Pursuant to the Asset Purchase Agreement, the Company paid VegasTix4Less \$2.0 million in cash and issued a \$2.0 million non-interest bearing secured promissory note. The secured promissory note is secured by the assets acquired from VegasTix4Less. As this obligation carries no interest, the Company imputed an average interest rate of 5.00% resulting in a discount of \$200,000, which is being amortized on an effective interest rate basis over the eight year term of the note. As of December 31, 2015, \$600,000 was outstanding under the promissory note. During the year ended December 31, 2016, the Company made a payment of \$200,000. As of December 31, 2016, \$400,000 was outstanding under the note payable, of which \$200,000 is due per year concluding in fiscal year 2018. As of December 31, 2016 and 2015, the unamortized discount for the note payable was \$24,000

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and \$48,000, resulting in a net obligation due of \$376,000 and \$552,000, of which \$200,000 and \$176,000 was reflected as part of current liabilities on the accompanying consolidated balance sheets, respectively.

**6. Obligation for Share Purchases**

In fiscal year 2011, certain officers, excluding the Company's Chairman and Chief Executive Officer, and employees of the Company (the "Purchasers") agreed to purchase an aggregate of 942,590 shares of the Company's common stock from existing stockholders at \$2.00 per share or an aggregate of purchase price \$1.9 million.

The selling stockholders agreed to defer the payment of their respective purchase prices in several installments over a five year period. The Company agreed to loan to the Purchasers an amount in cash sufficient to enable such Purchasers to pay the purchase price installment payments when due to the respective sellers under their respective purchase agreements.

The Company had recorded the aggregate purchase of \$2.1 million due from the Purchasers as a contra-equity account in the accompanying condensed consolidated balance sheets. The balance due from Purchasers was \$2.1 million as of December 31, 2014. As of December 31, 2014, \$159,000 was outstanding under the Company's purchase obligation.

In March 2015, pursuant to separate Repayment Agreements by and between the Company and each Purchaser ("Repayment Agreements"), the Company assumed and paid in full the remaining obligation of the respective Purchasers to the selling stockholders of approximately \$159,000 and acquired the remaining underlying shares from the selling stockholders. Each Repayment Agreement also provided for a return of shares to the Company (that were previously paid for and acquired from the selling stockholders) as payment in full for the loans previously provided by the Company to the given Purchaser to purchase the relevant shares from the selling stockholders. As a result of the execution of the separate Repayment Agreements, a total of 942,590 shares of the Company's common stock was returned to the Company's treasury, and the previously recorded \$2.1 million due from the Purchasers was reclassified to treasury stock.

**7. Commitments and Contingencies**

*Operating Lease Obligations*

The Company leases office space for its corporate headquarters in Studio City, California. Tix4Tonight leases space for its multiple ticket facilities and its administrative offices in Las Vegas, Nevada.

Many of the Company's operating leases contain predetermined fixed increases in the minimum rental rate during the initial lease term and/or rent holiday periods. For these leases, the Company recognizes the related rent expense on a straight-line basis beginning on the effective date of the lease. Some leases also contain provisions for additional rent based on sale levels. Total lease expense was \$3.7 million and \$3.7 million for the years ended December 31, 2016 and 2015, respectively.

At December 31, 2016, the Company's operating lease commitments for the next five fiscal years are summarized below.

<b>Years Ending December 31,</b>	<b>Amount</b>
2017	\$ 2,248,000
2018	2,136,000
2019	1,097,000
2020	127,000
Total	\$ 5,608,000

*Retirement Plan*

The Company has a 401(k) retirement plan which covers substantially all employees. Under the plan, participants may contribute up to 75% of pretax annual compensation, as defined in the Plan. Participants may also contribute amounts representing distributions from other qualified plans. If an employee enrolls, a participant's minimum deferral is 1% of eligible compensation of the participant. Participants who have attained age 50 before the end of the year are eligible to make catch-up contributions. The Company contributes 100% of the first 3% of compensation and then 50% of the next 2% of compensation that a participant contributes to the Plan. Additional discretionary matching contributions may be contributed at the discretion of the Company's



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Board of Directors. Contributions are subject to certain limitations of the Internal Revenue Code. Total 401(k) retirement plan expense amounted to \$116,000 and \$103,000 for the years ended December 31, 2016 and 2015, respectively.

## **8. Stockholders' Equity**

### **Stockholder Rights Agreement**

On January 2, 2014, the Company announced that its Board of Directors adopted an amendment of the Company's Stockholder Rights Agreement (the "Rights Agreement") to protect the interests of all Company stockholders by lowering the beneficial ownership threshold to a level that could help preserve the value of the Federal Net Operating Loss Carry Forwards ("NOLs"). The Company's ability to use the NOLs would be substantially limited if there were an "ownership change" as defined under Section 382 of the U.S. Internal Revenue Code and related U.S. Treasury regulations ("Section 382"). In general, an "ownership change" would occur under Section 382 if the Company's "5-percent stockholders," as defined under Section 382, collectively increase their ownership in the Company by more than 50 percentage points over a rolling three-year period.

Under the terms of the amended and restated Rights Agreement, subject to certain exceptions, in the event a person or group, without Board approval, acquires beneficial ownership of 4.95% or more of the outstanding common stock or announces a tender or exchange offer which would result in such person or group's beneficial ownership of 4.95% or more of the outstanding common stock (a "Triggering Stockholder"), then all stockholders of the Company (other than the Triggering Stockholder) will be entitled to acquire shares of common stock at a 50% discount (a "Dilution Event").

A person or group that owns 4.95% or more of the outstanding common stock at the time of the adoption of the amended and restated Rights Agreement (an "Existing Major Stockholder") will not trigger a Dilution Event. However, a Dilution Event will be triggered if an Existing Major Stockholder, without Board approval, acquires any additional shares of common stock. The 4.95% beneficial ownership threshold under the amended and restated Rights Agreement will remain applicable until March 31, 2021, or earlier, if the Board determines that the reduced threshold is no longer necessary for the preservation of the NOLs.

The foregoing description of the amended and restated Rights Agreement is qualified in its entirety by reference to the full text of the amended and restated Rights Agreement, a copy of which is available on the Company's website and is incorporated herein by reference.

### **Quarterly Cash Dividend Program**

In April 2015, the Company announced a program of paying a regular quarterly cash dividend to the Company's stockholders. During the year ended December 31, 2016 and 2015, the Company paid a total of \$3.7 million and \$2.6 million in cash dividends to its stockholders, respectively.

### **Treasury Shares**

During the year ended December 31, 2016, options to acquire 117,777 shares of common stock were exchanged on a cashless basis for the issuance of 53,693 shares of common stock. The Company agreed to pay the corresponding taxes on behalf of the option holders of \$39,000 in exchange for the return of 17,453 shares of common stock or \$2.23 per share. The Company accounted for the 17,453 shares as an acquisition of our treasury stock.

During the year ended December 31, 2015, options to acquire 1,206,406 shares of common stock were exchanged on a cashless basis for the issuance of 563,971 shares of common stock. The Company agreed to pay the corresponding taxes on behalf of these option holders of \$495,000 in exchange for the return of 225,560 shares of common stock or \$2.19 per share. The Company accounted for the 225,560 shares as treasury stock.

In March 2015, as a result of the execution of the separate Repayment Agreements (see Note 6 above), a total of 942,590 shares of the Company's common stock was returned to the Company's treasury.

## **9. Stock-Based Compensation Plans**

As of December 31, 2015, the Company has two stock-based compensation plans, which are described below.

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**2009 Equity Incentive Plan**

On July 8, 2009, the 2009 Equity Incentive Plan (the “2009 Equity Plan”) for officers, employees and consultants of the Company was approved pursuant to a Joint Written Consent of the Board of Directors and Majority Stockholders of the Company. The 2009 Equity Plan authorized the granting of not more than 3,000,000 restricted shares, stock appreciation rights (“SAR’s”), and incentive and non-qualified stock options to purchase shares of the Company’s common stock. The 2009 Equity Plan provided that stock options or SAR’s granted can be exercisable immediately as of the effective date of the applicable agreement, or in accordance with a schedule or performance criteria as may be set in the applicable agreement. The exercise price for non-qualified stock options or SAR’s would be the amount specified in the agreement, but shall not be less than the fair value of the Company’s common stock at the date of the grant. The exercise price for incentive stock options cannot be less than the fair market value of the Company’s common stock on the date of grant (110% of the fair market value of the Company’s common stock on the date of grant for a stockholder owning in excess of 10% of the Company’s common stock). The maximum term of options and SARs granted under the plan is ten years.

During the year ended December 31, 2016, the Company Company granted to its non-officer employees, stock options to purchase an aggregate of 172,000 shares of common stock at an average price of \$2.19 per share. The options were valued at \$108,000 and will vest over a 36 month period and have a ten year life. During the year ended December 31, 2015, the Company granted to an executive stock options to purchase an aggregate of 500,000 shares of common stock at an average price of \$1.30 per share. The options were valued at \$302,000 and will vest one-fifth on each anniversary of the grant date and has a five year life. As of December 31, 2016, options to purchase 21,000 shares of common stock remain reserved for issuance under the 2009 Equity Plan.

**Amended and Restated Directors Equity Incentive Plan (2004 Directors Option Plan)**

On March 3, 2005, the Company adopted the Directors Stock Option Plan (the “2004 Directors Option Plan”) for non-employee directors of the Company. The 2004 Directors Option Plan was approved pursuant to a Joint Written Consent of the Board of Directors and Majority Stockholders of the Company dated September 22, 2004. The 2004 Directors Option Plan authorized the granting of non-qualified stock options to purchase an aggregate of not more than 100,000 shares of the Company’s common stock. The 2004 Directors Option Plan provided that options granted would be exercisable for a period not to exceed ten years and would vest on a cumulative basis as to one-third of the total number of shares covered thereby at any time after one year from the date the option was granted and an additional one-third of such total number of shares at any time after the end of each consecutive one-year period thereafter until the option had become exercisable as to all of such total number of shares. The exercise price for non-qualified stock options would be the fair value of the Company’s common stock at the date of the grant. No option may be exercised during the first six months of its term except in the case of death. On May 30, 2007, an amendment to the 2004 Directors Option Plan was approved through a Corporate Resolution by the Company’s Board of Directors, and adjusts the vesting period of options granted from vesting one-third annually over three years to vesting immediately. On July 8, 2009, an additional amendment to the 2004 Directors Option Plan (“The Amendment”) was approved pursuant to a Joint Written Consent of the Board of Directors and Majority Stockholders of the Company. The Amendment increased the authorized amount of option grants to purchase shares of our common stock to 1,000,000.

On March 10, 2014, the Company amended and restated the 2004 Directors Option Plan and renamed it the “Amended and Restated Directors Equity Incentive Plan” (the “Directors Plan”). Awards under the Directors Plan may be made only to members of the Board of Directors who are not employees of the Company or any of its affiliates. The Directors Plan authorizes the issuance of not more than 1,000,000 shares of the Company’s common stock pursuant to awards of restricted shares, SAR’s, and non-qualified stock options. The Directors Plan provides that stock options or SAR’s granted can be exercisable immediately as of the effective date of the applicable agreement, or in accordance with a schedule or performance criteria as may be set in the applicable agreement. The exercise price for stock options or SAR’s would be the amount specified in the agreement, but would not be less than the fair value of the common stock at the date of the grant. The maximum term of options and SARs granted under the plan is 10 years.

During the years ended December 31, 2016 and 2015, the Company did not issue any options to purchase shares of its common stock under the Directors Plan. As of December 31, 2016, options to purchase 310,000 shares of common stock remain reserved for issuance under the Directors Plan.

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**Summary of Stock Options**

A summary of the combined stock options for the year ended December 31, 2016 for the two plans discussed above is as follows:

	<b>Number of Options</b>		<b>Weighted Average Exercise Price</b>
Balance outstanding, December 31, 2014	3,383,295	\$	1.78
Options granted	500,000		1.30
Options exercised	(1,225,850)		1.17
Options expired or forfeited	-		-
Balance outstanding, December 31, 2015	2,657,445		1.97
Options granted	422,000		1.95
Options exercised	(151,111)		1.22
Options expired or forfeited	(18,000)		2.19
Balance outstanding, December 31, 2016	2,910,334	\$	2.01
Balance exercisable, December 31, 2016	1,817,334	\$	2.32

On September 1, 2016, the Company entered into a new employment agreement with Kimberly Simon, the Company's Chief Operating Officer. Ms. Simon's prior employment agreement expired on August 31, 2016. As part of the new employment agreement, Ms. Simon received stock options to purchase an aggregate of 250,000 shares of Common Stock of which 50,000 vest and become exercisable on each anniversary date of the new employment agreement. The fair value of the options granted was determined to be \$86,070 and is being amortized over the vesting period of 60 months.

In March 2015, the Company entered into a new employment agreement with Mitch Francis, the Company's Chief Executive Officer. Mr. Francis' prior employment agreement expired on February 28, 2015. As part of the new employment agreement, Mr. Francis received stock options to purchase an aggregate of 500,000 shares of common stock of which 100,000 vest and become exercisable on each anniversary date of the new employment agreement. The fair value of the options granted was determined to be \$301,652 and is being amortized over the vesting period of 60 months.

During the year ended December 31, 2016, options to purchase 33,334 shares of common stock at \$1.25 per share were exercised for cash proceeds of \$42,000. Additionally, options to acquire 117,777 shares of common stock were exchanged on a cashless basis for the issuance of 53,693 shares of common stock.

During the year ended December 31, 2015, options to purchase 19,444 shares of common stock at \$1.25 per share were exercised for cash proceeds of \$25,000. Additionally, options to acquire 1,206,406 shares of common stock were exchanged on a cashless basis for the issuance of 563,971 shares of common stock.

The fair value of each option on the date of grant was estimated using the Black-Scholes option pricing model with the following weighted average assumptions:

	<b>2016</b>		<b>2015</b>	
Risk free rate of return	1.53	%	1.71	%
Option lives in years	7.00		7.00	
Annual volatility of stock price	66.04	%	77.00	%
Dividend yield	11.00	%	10.53	%

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Information relating to outstanding stock options at December 31, 2016, summarized by exercise price, is as follows:

Exercise Price Per Share	Outstanding			Exercisable	
	Shares	Life (Years)	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
\$1.00 - \$1.99	2,423,334	4.62	\$ 1.31	1,445,834	\$ 1.25
\$2.00 - \$2.99	154,000	9.23	\$ 2.19	38,500	\$ 2.19
\$6.00 - \$7.00	333,000	0.73	\$ 6.99	333,000	\$ 6.99
	<u>2,910,334</u>	<u>4.42</u>	<u>\$ 2.01</u>	<u>1,817,334</u>	<u>\$ 2.32</u>

The Company recorded compensation expense pursuant to authoritative guidance provided by the ASC Topic 718 – *Stock Compensation* for the years ended December 31, 2016 and 2015 of \$404,000 and \$358,000, respectively. As of December 31, 2016, the Company has outstanding unvested options with future compensation costs of \$567,000, which will be recorded as compensation cost as the options vest over their remaining average vesting period of 2.36 years.

The intrinsic value of outstanding stock options at December 31, 2016 was \$676,000 as compared to \$2.1 million at December 31, 2015. The intrinsic value of exercisable stock options at December 31, 2016 was \$460,000 as compared to \$888,000 at December 31, 2015.

#### Summary of Warrants

A summary of warrant activity for the year ended December 31, 2016 is as follows:

	Number of warrants	Weighted average exercise price
Balance outstanding, December 31, 2014	747,059	\$ 1.33
Warrants granted	-	-
Warrants exercised	-	-
Warrants expired	-	-
Balance outstanding, December 31, 2015	747,059	1.33
Warrants granted	-	-
Warrants exercised	-	-
Warrants expired	-	-
Balance outstanding, December 31, 2016	<u>747,059</u>	<u>\$ 1.33</u>
Balance exercisable, December 31, 2016	<u>747,059</u>	<u>\$ 1.33</u>

Information relating to outstanding warrants at December 31, 2016, summarized by exercise price, is as follows:

Exercise Price Per Share	Outstanding			Exercisable	
	Shares	Life (Years)	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
\$1.20 - \$1.85	<u>747,059</u>	<u>3.21</u>	<u>\$ 1.33</u>	<u>747,059</u>	<u>\$ 1.33</u>

The Company recorded compensation expense pursuant to authoritative guidance provided by the ASC Topic 718 – *Stock Compensation* for the year ended December 31, 2015 of \$8,000. As of December 31, 2016, the Company has no outstanding unvested warrants with future compensation costs.

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The intrinsic value of outstanding warrants at December 31, 2016 was \$222,000 as compared to \$614,000 at December 31, 2015. The intrinsic value of exercisable warrants at December 31, 2016 was \$181,000 as compared to \$614,000 at December 31, 2015.

# **10. Related Party Transactions**

During the year ended December 31, 2016, options to acquire 117,777 shares of common stock were exchanged on a cashless basis for the issuance of 53,693 shares of common stock. The Company agreed to pay the corresponding taxes on behalf of the option holders of \$39,000 in exchange for the return of 17,453 shares of common stock or \$2.23 per share. The Company accounted for the 17,453 shares as an acquisition of our treasury stock (See Note 8 above).

During the year ended December 31, 2015, options to acquire 1,206,406 shares of common stock were exchanged on a cashless basis for the issuance of 563,971 shares of common stock. The Company agreed to pay the corresponding taxes on behalf of these option holders of \$495,000 in exchange for the return of 225,560 shares of common stock or \$2.19 per share. The Company accounted for the 225,560 shares as a part of our treasury stock (See Note 8 above).

Kimberly Simon, the Company's Chief Operating Officer, is the founder, managing director, and trustee of KiSS for Homeless Animals, an Internal Revenue Service section 501(c)(3) tax-exempt organization, whose charter is to help homeless animals in need. Mitch Francis, the Company's Chairman and Chief Executive Officer, is a Trustee. During the year ended December 31, 2016 and 2015, the Company made charitable contributions to KiSS for Homeless Animals of \$44,000 and \$57,000, respectively.

In March 2015, pursuant to separate Repayment Agreements by and between the Company and each Purchaser described in Note 6 above, the Company assumed and paid in full the remaining obligation of the respective Purchasers to the selling stockholders of approximately \$159,000 and acquired the remaining underlying shares from the selling stockholders. Each Repayment Agreement also provided for a return of shares to the Company (that were previously paid for and acquired from the selling stockholders) as payment in full for the loans previously provided by the Company to the given Purchaser to purchase the relevant shares from the selling stockholders. As a result of the execution of the separate Repayment Agreements, a total of 942,590 shares of the Company's common stock was returned to the Company's treasury, and the previously recorded \$2.1 million due from the Purchasers was reclassified to treasury stock.

# **11. Income Taxes**

For the years ended December 31, 2016 and 2015, we recognized income tax expense (benefit from) comprised of the following:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Federal income tax	35.00%	35.00%
Federal alternative minimum tax	2.00%	2.00%
State income tax, net of federal benefit	0.22%	0.22%
Changes in valuation allowance	-%	(241.64)%
Provision for (benefit from) for income taxes	<u>37.22%</u>	<u>(204.42)%</u>

A reconciliation of the statutory U.S. federal rate and effective rates is as follows:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Federal current tax	\$ 104,000	\$ 254,000
State current tax	1,000	1,000
Federal deferred tax	<u>1,023,000</u>	<u>(11,531,000)</u>
Provision for (benefit from) income taxes	<u>\$ 1,128,000</u>	<u>\$ (11,276,000)</u>

Our deferred tax assets are comprised of the following:

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	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
<b>Deferred Tax Assets:</b>		
Net operating losses	\$ 9,395,000	\$ 10,385,000
Other	1,806,000	1,839,000
Total	11,201,000	12,224,000
Valuation allowance	(693,000)	(693,000)
<b>Net Deferred Tax Asset</b>	<b>\$ 10,508,000</b>	<b>\$ 11,531,000</b>

At December 31, 2016, the Company estimates it had federal net operating loss carry forwards (“NOLs”) of approximately \$25.7 million, which are subject to certain limitations, which begin expiring in 2017 in varying amounts through 2032.

Authoritative guidance issued by the ASC Topic 740 – *Income Taxes* requires that a valuation allowance be established when it is more likely than not that all or a portion of deferred tax assets will not be realized. Based on a study performed by an outside third party during the third quarter of 2011 and due to the restrictions imposed by Internal Revenue Code Section 382 regarding substantial changes in ownership of companies with loss carry forwards, the utilization of the Company’s NOL is limited to \$1.8 million per year as a result of recent cumulative changes in stock ownership. NOL’s of \$23.5 million, which were incurred subsequent to the latest change in control, are not subject to the \$1.8 million per year limitation.

Prior to 2015, we recorded a full valuation allowance on our deferred tax assets to reduce the deferred tax assets to the amount that was believed more likely than not to be realized. In assessing the need for a valuation allowance, we considered all available positive and negative evidence, including past results, the existence of cumulative losses in prior years, substantial historical changes in ownership, and forecasted future taxable income. During 2015, the majority of our valuation allowance, primarily related to NOLs, was reversed based on historical earnings and forecasts of future taxable income, resulting in the recognition of a \$11.5 million tax benefit.

We consider all evidence available when determining whether deferred tax assets are more likely-than-not to be realized, including projected future taxable income, scheduled reversals of deferred tax liabilities, prudent tax planning strategies, and recent financial operations. The evaluation of this evidence requires significant judgement about the forecast of future taxable income is consistent with the plans and estimates we are using to manage the underlying business. In evaluating the objective evidence that historical results provide, we consider three years of cumulative operating income. As of December 31, 2016, we have determined that deferred tax assets of \$693,000 do not meet the requirements to be realized and have a valuation allowance against them.

We file consolidated income tax returns in the U.S. federal jurisdiction, and in California. With limited exception including our NOL, we are no longer subject to U.S. federal, state and local, by tax authorities for years before 2012. We do not anticipate the results of any open examinations would result in a material change to our financial position.

## **12. Legal Proceedings**

We are engaged from time to time in the defense of lawsuits arising out of the ordinary course and conduct of our business. There is no action, suit, proceeding, inquiry or investigation before or by any court, public board, government agency, self-regulatory organization or body pending or, to the knowledge of the executive officers of our Company or our subsidiary, threatened against our Company, our common stock, our subsidiary or of our Company or our subsidiary’s officers or directors in their capacities as such.

## **13. Subsequent Events**

The Company has evaluated subsequent events occurring from January 1, 2017 through February 21, 2017, the date the financial statements were issued.

On January 4, 2017, the Company announced a cash dividend of \$0.055 per share to be paid on January 30, 2017 to stockholders of record on January 16, 2017.

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On January 24, 2017, the Company modified the term of a warrant originally granted to its Chief Executive Officer in March 2012 and due to expire in March 2017. The Company extended the expiration date of the warrant by an additional 60 months. Due to the modification, the Company recorded an charge of \$31,000 on the modification date to account for the incremental change in fair value of the warrants before and after the modification.