

CLOUDCOMMERCE, INC.
Form 10-Q
August 14, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For quarterly period ended June 30, 2018.

or

TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Transition period from _____ to _____

Commission
File
Number: 000-13215

**CLOUDCOMMERCE,
INC.**

(Exact name of registrant as
specified in its charter)

NEVADA 30-0050402
(State or other (I.R.S.
jurisdiction of Employer
incorporation or Identification)

organization) No.)

**1933 Cliff Drive, Suite 1,
Santa Barbara, CA 93109**

(Address of principal
executive offices) (Zip Code)

(805) 964-3313

Registrant's telephone
number, including area code

(Former name, former
address and former fiscal
year, if changed since last
report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

| | |
|---|---|
| Large accelerated filer | Accelerated filer |
| Non-accelerated filer (Do not check if a smaller reporting company) | Smaller reporting company <input checked="" type="checkbox"/> |
| | Emerging growth company |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Table of Contents

Indicate the number of shares outstanding of each of the issuer’s classes of common stock as of the latest practicable date.

As of August 14, 2018, the number of shares outstanding of the registrant’s class of common stock was 136,279,079.

Table of Contents

| PART I – FINANCIAL INFORMATION | Page |
|---|-------------|
| Item 1. <u>Condensed Consolidated Financial Statements</u> | 3 |
| <u>Condensed Consolidated Balance Sheets as of June 30, 2018 (unaudited) and December 31, 2017</u> | 4 |
| <u>Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2018 and June 30, 2017 (unaudited)</u> | 5 |
| <u>Condensed Consolidated Statement of Shareholders’ Equity for the six months ended June 30, 2018 (unaudited)</u> | 6 |
| <u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2018 and June 30, 2017 (unaudited)</u> | 7 |
| <u>Notes to Condensed Consolidated Financial Statements (unaudited)</u> | 8 |
| Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 26 |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 31 |
| Item 4. <u>Controls and Procedures</u> | 31 |
| PART II - OTHER INFORMATION | |
| Item 1. <u>Legal Proceedings</u> | 32 |
| Item 1A. <u>Risk Factors</u> | 32 |
| Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 32 |
| Item 3. <u>Defaults Upon Senior Securities</u> | 32 |
| Item 4. <u>Mine Safety Disclosures</u> | 32 |

| | |
|----------------------------------|----|
| Item 5. <u>Other Information</u> | 32 |
| Item 6. <u>Exhibits</u> | 32 |
| <u>Signatures</u> | 33 |

Table of Contents

PART I. - FINANCIAL INFORMATION

Item 1. CONSOLIDATED FINANCIAL STATEMENTS

3

Table of Contents

CLOUDCOMMERCE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

| | June 30, 2018 (unaudited) | December 31, 2017 |
|--|------------------------------|----------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash | \$743,764 | \$272,321 |
| Accounts receivable, net | 1,218,737 | 877,570 |
| Accounts receivable, net - related party | 148,024 | 398,410 |
| Prepaid and other current Assets | 82,972 | 39,168 |
| TOTAL CURRENT ASSETS | 2,193,497 | 1,587,469 |
| PROPERTY & EQUIPMENT, net | 148,295 | 161,325 |
| OTHER ASSETS | | |
| Lease deposit | 18,600 | 13,300 |
| Goodwill and other intangible assets, net | 10,184,403 | 9,546,757 |
| TOTAL OTHER ASSETS | 10,203,003 | 9,560,057 |
| TOTAL ASSETS | \$12,544,795 | \$11,308,851 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$1,206,464 | \$1,004,203 |
| Accrued expenses | 641,323 | 522,794 |
| Lines of credit | 484,173 | 475,468 |
| Deferred income and customer deposit | 710,893 | 620,504 |
| Convertible notes and interest payable, current, net | 277,801 | 97,013 |
| Capital lease obligation, current | 32,382 | 32,382 |
| Notes payable | 750,000 | — |
| Notes payable, related parties | 1,657,020 | 670,819 |
| TOTAL CURRENT LIABILITIES | 5,760,056 | 3,423,183 |
| LONG TERM LIABILITIES | | |
| Capital lease obligation, long term | 38,704 | 54,693 |
| Deferred tax liability | 910,780 | 1,021,566 |
| Accrued expenses, long term | 205,703 | 207,803 |
| TOTAL LONG TERM LIABILITIES | 1,155,187 | 1,284,062 |
| TOTAL LIABILITIES | 6,915,243 | 4,707,245 |
| COMMITMENTS AND CONTINGENCIES (see Note 13) | — | — |
| SHAREHOLDERS' EQUITY | | |
| Preferred stock, \$0.001 par value; | | |

Edgar Filing: CLOUDCOMMERCE, INC. - Form 10-Q

| | | |
|--|----------------------|----------------------|
| 5,000,000 Authorized shares: | | |
| Series A Preferred stock; 10,000 authorized, 10,000 shaes issued and outstanding; | 10 | 10 |
| Series B Preferred stock; 25,000 authorized, 18,025 shares issued and outstanding; | 18 | 18 |
| Series C Preferred Stock; 25,000 authorized, 14,425 shares issued and outstanding; | 14 | 14 |
| Series D Preferred Stock; 90,000 authorized, 90,000 shares issued and outstanding; | 90 | 90 |
| Series E Preferred stock; 10,000 authorized, 10,000 shares issued and outstanding; | 10 | 10 |
| Common stock, \$0.001 par value; | | |
| 2,000,000,000 authorized shares; 136,279,079 and 130,252,778 shares issued and outstanding, respectively | 136,279 | 130,252 |
| Additional paid in capital | 29,268,409 | 29,094,147 |
| Accumulated deficit | (23,775,278) | (22,622,935) |
| TOTAL SHAREHOLDERS' EQUITY | 5,629,552 | 6,601,606 |
| | | |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | \$ 12,544,795 | \$ 11,308,851 |

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

CLOUDCOMMERCE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|---------------|------------------|----------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| REVENUE | \$2,050,766 | \$723,817 | \$3,446,042 | \$1,209,925 |
| REVENUE - related party | 546,884 | — | 2,028,317 | — |
| TOTAL REVENUE | 2,597,650 | 723,817 | 5,474,359 | 1,209,925 |
| OPERATING EXPENSES | | | | |
| Salaries and outside services | 1,462,011 | 784,862 | 2,952,351 | 1,563,455 |
| Selling, general and administrative expenses | 1,128,626 | 209,432 | 2,933,804 | 460,461 |
| Stock based compensation | 125,904 | 124,836 | 285,976 | 248,937 |
| Depreciation and amortization | 254,791 | 117,170 | 508,186 | 180,081 |
| TOTAL OPERATING EXPENSES | 2,971,332 | 1,236,300 | 6,680,317 | 2,452,934 |
| LOSS FROM OPERATIONS BEFORE OTHER INCOME AND TAXES | (373,682) | (512,483) | (1,205,958) | (1,243,009) |
| OTHER INCOME (EXPENSE) | | | | |
| Other expense | (39,506) | (14,111) | (63,126) | (13,072) |
| Loss on sale of fixed assets | — | (1,567) | (22,358) | (1,567) |
| Gain on extinguishment of debt | 5,750 | | 5,750 | |
| Interest expense | (59,336) | (33,024) | (102,437) | (63,783) |
| TOTAL OTHER INCOME (EXPENSE) | (93,092) | (48,702) | (182,171) | (78,422) |
| LOSS FROM OPERATIONS BEFORE PROVISION FOR TAXES | (466,774) | (561,185) | (1,388,129) | (1,321,431) |
| PROVISION (BENEFIT) FOR INCOME TAXES | (105,795) | (400) | (235,786) | (400) |
| NET LOSS | (360,979) | (560,785) | (1,152,343) | (1,321,031) |
| PREFERRED DIVIDENDS | 75,315 | 20,000 | 129,794 | 40,000 |
| NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS | \$(436,294) | \$(580,785) | \$(1,282,137) | \$(1,361,031) |

Edgar Filing: CLOUDCOMMERCE, INC. - Form 10-Q

NET LOSS PER SHARE

| | | | | | |
|---------|----------|------------|------------|------------|---|
| BASIC | \$ (0.00 |) \$ (0.01 |) \$ (0.01 |) \$ (0.01 |) |
| DILUTED | \$ (0.00 |) \$ (0.01 |) \$ (0.01 |) \$ (0.01 |) |

WEIGHTED-AVERAGE COMMON SHARES

OUTSTANDING

| | | | | |
|---------|-------------|-------------|-------------|-------------|
| BASIC | 135,195,699 | 130,252,778 | 132,710,431 | 129,899,595 |
| DILUTED | 135,195,699 | 130,252,778 | 132,710,431 | 129,899,595 |

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

CLOUDCOMMERCE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

| | Preferred Stock | | Common Stock | | Additional | Accumulated | Total |
|--------------------------------------|-----------------|--------|--------------|------------|--------------------|----------------|--------------|
| | Shares | Amount | Shares | Amount | Paid-in Capital | Deficit | |
| Balance, December 31, 2017 | 142,450 | \$ 142 | 130,252,778 | \$ 130,252 | \$ 29,094,147 | \$(22,622,935) | \$ 6,601,606 |
| Conversion of convertible note | — | — | 6,026,301 | 6,027 | 18,079 | — | 24,106 |
| Dividend on Series A Preferred stock | — | — | — | — | (40,000) | — | (40,000) |
| Dividend on Series D Preferred stock | — | — | — | — | (89,793) | — | (89,793) |
| Stock based compensation | — | — | — | — | 285,976 | — | 285,976 |
| Net loss | — | — | — | — | — | (1,152,343) | (1,152,343) |
| Balance, June 30, 2018 (unaudited) | 142,450 | \$ 142 | 136,279,079 | \$ 136,279 | \$ 29,268,409 | \$(23,775,278) | \$ 5,629,552 |

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

CLOUDCOMMERCE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

| | Six Months Ended | |
|--|-------------------|-------------------|
| | June 30, 2018 | June 30, 2017 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net loss | | \$(1,321,031) |
| Adjustment to reconcile net loss to net cash (used in) operating activities | | |
| Depreciation and amortization | 508,186 | 180,081 |
| Bad debt expense | 68,029 | (41,467) |
| Stock based compensation | 285,976 | 248,937 |
| Loss on sale of fixed assets | 22,358 | 1,567 |
| Gain on extinguishment of debt | (5,750) | — |
| Change in assets and liabilities: | | |
| (Increase) Decrease in: | | |
| Accounts receivable | (158,810) | (43,908) |
| Prepaid and other assets | (43,804) | (1,898) |
| Lease deposit | (5,300) | — |
| Increase (Decrease) in: | | |
| Accounts payable | 202,261 | (17,488) |
| Accrued expenses | 183,701 | 61,355 |
| Capital lease obligation | (16,503) | — |
| Deferred income | 47,751 | 579,260 |
| Deferred tax liability | (235,786) | — |
| NET CASH USED IN OPERATING ACTIVITIES | (300,034) | (354,592) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of property and equipment | (41,304) | (6,025) |
| Proceeds from the sale of property and equipment | 20,658 | — |
| NET CASH USED IN INVESTING ACTIVITIES | (20,646) | (6,025) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Dividend paid | (93,132) | (40,000) |
| Net proceeds (payments) on line of credit | 8,705 | 28,659 |
| Payments on capital lease obligation | (9,000) | — |
| Payments on promissory notes | (255,450) | — |
| Proceeds from issuance of notes payable | 1,141,000 | 386,000 |

| | | |
|---|-----------|----------|
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 792,123 | 374,659 |
| NET INCREASE IN CASH | 471,443 | 14,042 |
| CASH, BEGINNING OF PERIOD | 272,321 | 16,827 |
| CASH, END OF PERIOD | \$743,764 | \$30,869 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | |
| Interest paid | \$71,074 | \$31,119 |
| Taxes paid | \$16,156 | \$3,629 |
| Conversion of notes payable to common stock | \$24,106 | \$— |

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

CLOUDCOMMERCE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

JUNE 30, 2018

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of CloudCommerce, Inc. (“CloudCommerce,” “we,” “us,” or the “Company”), have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all normal recurring adjustments considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. For further information, refer to the financial statements and footnotes thereto included in the Company's transition report Form 10-KT for the transition period from July 1, 2017 to December 31, 2017.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of CloudCommerce is presented to assist in understanding the Company's financial statements. The financial statements and notes are representations of the Company's management, which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.

The Consolidated Financial Statements include the Company and its wholly owned subsidiaries, Indaba Group, Inc., a Delaware corporation (“Indaba”), Parscale Digital, Inc., a Nevada corporation (“Parscale Digital”), WebTegrity, Inc., a Nevada corporation, Data Propria, Inc., a Nevada corporation (“Data Propria”), Parscale Media, LLC, a Texas limited liability company (“Parscale Media”), and Giles Design Bureau, Inc., a Nevada corporation (“Giles Design Bureau”). All significant inter-company transactions are eliminated in consolidation.

Accounts Receivable

The Company extends credit to its customers, who are located nationwide. Accounts receivable are customer obligations due under normal trade terms. The Company performs continuing credit evaluations of its customers' financial condition. Management reviews accounts receivable on a regular basis, based on contracted terms and how recently payments have been received to determine if any such amounts will potentially be uncollected. The Company includes any balances that are determined to be uncollectible in its allowance for doubtful accounts. After all attempts to collect a receivable have failed, the receivable is written off. The balance of the allowance account at June 30, 2018 and December 31, 2017 are \$74,213 and \$6,184 respectively.

On November 30, 2016, the Company entered into an agreement with a third party to sell the rights, with recourse, to accounts receivable amounts due from our customers to Indaba. Under the terms of the agreement, the Company may receive advances in amounts up to \$400,000, based on the amounts we invoice our customers, for a period of one year. Because the Company maintains the collectability risk of all outstanding balances, we record the amounts due from customers as a secured borrowing arrangement, with the customer balances at fair value in accounts receivable, including an allowance for any balances at risk of collectability, and the amount due to the third party as a liability. On

March 23, 2017, the Company amended the secured borrowing arrangement, which increased the maximum allowable balance by \$100,000, to a total of \$500,000. As of June 30, 2018, the balance due from this arrangement was \$101,326.

On October 19, 2017, the Company entered into an agreement with a third party to sell the rights, with recourse, to accounts receivable amounts due from our customers to Parscale Digital. Under the terms of the agreement, the Company may receive advances in amounts up to \$500,000, based on the amounts we invoice our customers, for a period of one year. Because the Company maintains the collectability risk of all outstanding balances, we record the amounts due from customers as a secured borrowing arrangement, with the customer balances at fair value in accounts receivable, including an allowance for any balances at risk of collectability, and the amount due to the third party as a liability. On April 12, 2018, the Company amended the secured borrowing arrangement, which increased the maximum allowable balance by \$250,000, to a total of \$750,000. As of June 30, 2018, the balance due from this arrangement was \$382,847.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements. Significant estimates made in preparing these financial statements include revenue recognition, the allowance

Table of Contents

for doubtful accounts, long-lived assets, intangible assets, business combinations, the deferred tax valuation allowance, and the fair value of stock options and warrants. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. As of June 30, 2018, the Company held cash and cash equivalents in the amount of \$743,764, which was held in the operating bank accounts. Of this amount, \$709,668 was held in the CloudCommerce bank account. Since this amount exceeds the FDIC insured limit of \$250,000, the balance at risk was \$459,668.

Revenue Recognition

The Company recognizes income when the service is provided or when product is delivered. We present revenue, net of customer incentives. Most of the income is generated from professional services and site development fees. We provide online marketing services that we purchase from third parties. The gross revenue presented in our statement of operations includes digital advertising revenue. We also offer professional services such as development services. The fees for development services with multiple deliverables constitute a separate unit of accounting in accordance with ASC 605-25, which are recognized as the work is performed. Upfront fees for development services or other customer services are deferred until certain implementation or contractual milestones have been achieved. If we have performed work for our clients, but have not invoiced clients for that work, then we record the value of the work in either deferred revenue, as a negative liability balance, or as an asset in costs in excess of billings. The terms of services contracts generally are for periods of less than one year. The deferred revenue and customer deposits as of June 30, 2018 and December 31, 2017 was \$710,893 and \$620,504, respectively.

We always strive to satisfy our customers by providing superior quality and service. Since we typically bill based on a Time and Materials basis, there are no returns for work delivered. When discrepancies or disagreements arise, we do our best to reconcile those by assessing the situation on a case-by-case basis and determining if any discounts can be given. Historically, no significant discounts have been granted.

Included in revenue are costs that are reimbursed by our clients, including third party services, such as photographers and stylists, furniture, supplies, and the largest component, digital advertising. We have determined, based on our review, that the amounts classified as reimbursable costs should be recorded as gross, due to the following factors:

- The Company is the primary obligor in the arrangement;
- We have latitude in establishing price;
- We have discretion in supplier selection; and
- The Company has credit risk.

During the six months ended June 30, 2018 and 2017, we included \$1,813,527 and zero, respectively, in revenue, related to reimbursable costs.

The Company records revenue into the following five categories:

- Data Sciences – Includes polling, research, modeling, data fees, consulting and reporting.
- Design – Includes branding, photography, copyrighting, printing, signs and interior design.
- Development – Includes website coding.
- Digital Advertising – Includes ad spend, SEO management and digital ad support.
- Other – Includes domain name management, account management, email marketing, web hosting, email hosting, client training, reimbursed expenses and partner commissions.

Table of Contents

For the six months ended June 30, 2018 and 2017, revenue was disaggregated into the five categories as follows:

| | Six months ended June 30, 2018 | | | Six months ended June 30, 2017 | | |
|---------------------|--------------------------------|-----------------|-------------|--------------------------------|-----------------|-------------|
| | Third Parties | Related Parties | Total | Third Parties | Related Parties | Total |
| Data Sciences | \$226,100 | \$20,000 | \$246,100 | \$— | \$ — | \$— |
| Design | 948,012 | 154,731 | 1,102,743 | — | — | — |
| Development | 780,941 | 111,879 | 892,820 | 1,128,658 | — | 1,128,658 |
| Digital Advertising | 1,013,738 | 1,544,015 | 2,557,753 | — | — | — |
| Other | 477,251 | 197,692 | 674,943 | 81,267 | — | 81,267 |
| Total | \$3,446,042 | \$2,028,317 | \$5,474,359 | \$1,209,925 | \$ — | \$1,209,925 |

Research and Development

Research and development costs are expensed as incurred. Total research and development costs were zero for the six months ended June 30, 2018 and 2017.

Advertising Costs

The Company expenses the cost of advertising and promotional materials when incurred. Total advertising costs were \$30,449 and \$3,316 for the six months ended June 30, 2018 and 2017, respectively.

Fair value of financial instruments

The Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities are carried at cost, which approximates their fair value, due to the relatively short maturity of these instruments. As of June 30, 2018 and December 31, 2017, the Company's notes payable have stated borrowing rates that are consistent with those currently available to the Company and, accordingly, the Company believes the carrying value of these debt instruments approximates their fair value.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 established a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). These tiers include:

- Level 1, defined as observable inputs such as quoted prices for identical instruments in active markets;
- Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable such as quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active; and
- Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions, such as valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

As of June 30, 2018 and December 31, 2017, the Company had no assets or liabilities that are required to be valued on a recurring basis.

Property and Equipment

Property and equipment are stated at cost, and are depreciated or amortized using the straight-line method over the following estimated useful lives:

| | |
|---------------------------------|---------------------|
| Furniture, fixtures & equipment | 7 Years |
| Computer equipment | 5 Years |
| Commerce server | 5 Years |
| Computer software | 3 - 5 Years |
| Leasehold improvements | Length of the lease |

Table of Contents

Depreciation expenses were \$20,832 and \$13,075 for the six months ended June 30, 2018 and 2017, respectively.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of a long-lived asset, management evaluates whether the estimated future undiscounted net cash flows from the asset are less than its carrying amount. If impairment is indicated, the long-lived asset would be written down to fair value. Fair value is determined by an evaluation of available price information at which assets could be bought or sold, including quoted market prices, if available, or the present value of the estimated future cash flows based on reasonable and supportable assumptions.

Indefinite Lived Intangibles and Goodwill Assets

The Company accounts for business combinations under the acquisition method of accounting in accordance with ASC 805, "Business Combinations," where the total purchase price is allocated to the tangible and identified intangible assets acquired and liabilities assumed based on their estimated fair values. Significant estimates in valuing certain intangible assets include, but are not limited to, future expected cash flows from acquired customer lists, acquired technology, and trade names from a market participant perspective, useful lives and discount rates. Management's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. The purchase price is allocated using the information currently available, and may be adjusted, up to one year from acquisition date, after obtaining more information regarding, among other things, asset valuations, liabilities assumed and revisions to preliminary estimates. The purchase price in excess of the fair value of the tangible and identified intangible assets acquired less liabilities assumed is recognized as goodwill.

The Company tests for indefinite lived intangibles and goodwill impairment in the fourth quarter of each year and whenever events or circumstances indicate that the carrying amount of the asset exceeds its fair value and may not be recoverable. In accordance with its policies, the Company performed a qualitative assessment of indefinite lived intangibles and goodwill at December 31, 2017, and determined there was impairment of indefinite lived intangibles and goodwill from our Indaba acquisition. Accordingly, all intangible assets and goodwill related to the Indaba acquisition has been written off, amounting to \$1,239,796.

Business Combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair value, at the acquisition date, of assets received, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. Any costs directly attributable to the business combination are expensed in the period incurred. The acquiree's identifiable assets and liabilities are recognized at their fair values at the acquisition date.

Goodwill arising on acquisition is recognized as an asset and initially measured at cost, being the excess of the cost of the business combination over the Company's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognized.

Concentrations of Business and Credit Risk

The Company operates in a single industry segment. The Company markets its services to companies and individuals in many industries and geographic locations. The Company's operations are subject to rapid technological advancement and intense competition. Accounts receivable represent financial instruments with potential credit risk. The Company typically offers its customers credit terms. The Company makes periodic evaluations of the credit worthiness of its enterprise customers and other than obtaining deposits pursuant to its policies, it generally does not require collateral. In the event of nonpayment, the Company has the ability to terminate services. As of June 30, 2018, the Company held cash and cash equivalents in the amount of \$743,764, which was held in the operating bank accounts. Of this amount, \$709,668 was held in the CloudCommerce bank account. Since this amount exceeds the FDIC insured limit of \$250,000, the balance at risk was \$459,668.

Stock-Based Compensation

The Company addressed the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for either equity instruments of the enterprise or liabilities that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. The transactions are accounted for using a fair-value-based method and recognized as expenses in our statement of operations.

Table of Contents

Stock-based compensation expense recognized during the period is based on the value of the portion of stock-based payment awards that is ultimately expected to vest. Stock-based compensation expense recognized in the consolidated statement of operations during the six months ended June 30, 2018, included compensation expense for the stock-based payment awards granted prior to, but not yet vested, as of June 30, 2018 based on the grant date fair value estimated. Stock-based compensation expense recognized in the statement of operations for the six months ended June 30, 2018 is based on awards ultimately expected to vest, or has been reduced for estimated forfeitures. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The stock-based compensation expense recognized in the consolidated statements of operations during the six months ended June 30, 2018, and 2017 were \$285,976 and \$248,937, respectively.

Basic and Diluted Net Income (Loss) per Share Calculations

Income (Loss) per Share dictates the calculation of basic earnings per share and diluted earnings per share. Basic earnings per share are computed by dividing income available to common shareholders by the weighted-average number of common shares available. Diluted earnings per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. The shares for employee options, warrants and convertible notes were used in the calculation of the income per share.

For the six months ended June 30, 2018, the Company has excluded 154,800,000 shares of common stock underlying options, 10,000 Series A Preferred shares convertible into 100,000,000 shares of common stock, 18,025 Series B Preferred shares convertible into 450,625,000 shares of common stock, 14,425 Series C Preferred shares convertible into 144,250,000 shares of common stock, 90,000 Series D Preferred shares convertible into 225,000,000 shares of common stock, 10,000 Series E Preferred shares convertible into 20,000,000 shares of common stock and 39,158,500 shares of common stock underlying \$277,801 in convertible notes, because their impact on the loss per share is anti-dilutive.

For the six months ended June 30, 2017, the Company has excluded 123,000,000 shares of common stock underlying options, 10,000 Series A Preferred shares convertible into 100,000,000 shares of common stock, 18,025 Series B Preferred shares convertible into 450,625,000 shares of common stock, and 23,421,500 shares of common stock underlying \$93,686 in convertible notes, because their impact on the loss per share is anti-dilutive.

Dilutive per share amounts are computed using the weighted-average number of common shares outstanding and potentially dilutive securities, using the treasury stock method if their effect would be dilutive.

Recently Issued Accounting Pronouncements

Management reviewed accounting pronouncements issued during the six months ended June 30, 2018, and the following pronouncements were adopted during the period.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers* (“ASU 2014-09”). The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. The standard is effective for annual periods beginning after December 15, 2017, and interim periods therein. The Company follows paragraph 606 of the FASB Accounting Standards Codification for revenue recognition and ASU 2014-09, adopting the pronouncements on January 1, 2018. The company considers revenue realized or realizable and earned when services are performed to such a degree that the performed service is delivered or deliverable to the client, or when a tangible item, such as interior décor or signage, is delivered to the client. Since the Company was already

recognizing revenue in a manner consistent with paragraph 606 of the FASB Accounting Standards Codification, there was no material impact on prior year results.

ASU 2014-09 supersedes existing guidance on revenue recognition with a five-step model for recognizing and measuring revenue from contracts with customers. The objective of the new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows. The guidance can be applied retrospectively to each prior reporting period presented (full retrospective method) or retrospectively with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of initial adoption (modified retrospective method). The Company adopted the new standard effective January 1, 2018 using the modified retrospective method applied to those contracts that were not completed or substantially completed as of January 1, 2018. The timing and measurement of revenue

Table of Contents

recognition under the new standard is not materially different than under the old standard. The adoption of the new standard did not have an impact on the Company's consolidated financial statements.

In January 2017, the FASB issued 2017-04, *Intangibles - Goodwill and Other* (Topic 350): Simplifying the Test for Goodwill Impairment. The amendments in this ASU simplify the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test and eliminating the requirement for a reporting unit with a zero or negative carrying amount to perform a qualitative assessment. Instead, under this pronouncement, an entity would perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and would recognize an impairment change for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized is not to exceed the total amount of goodwill allocated to that reporting unit. In addition, income tax effects will be considered, if applicable. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating the impact of this ASU on its consolidated financial statements and related disclosures.

Income Taxes

The Company uses the liability method of accounting for income taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to financial statements carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. The measurement of deferred tax assets and liabilities is based on provisions of applicable tax law. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance based on the amount of tax benefits that, based on available evidence, is not expected to be realized.

3. LIQUIDITY AND OPERATIONS

The Company had net loss of \$1,152,343 for the six months ended June 30, 2018, and \$1,321,031 for the six months ended June 30, 2017, and net cash used in operating activities of \$300,034 and \$354,592, in the same periods, respectively.

While the Company expects that its capital needs in the foreseeable future may be met by cash-on-hand and projected positive cash-flow, there is no assurance that the Company will be able to generate enough positive cash flow or have sufficient capital to finance its growth and business operations, or that such capital will be available on terms that are favorable to the Company or at all. In the current financial environment, it could become difficult for the Company to obtain working capital and other business financing. There is no assurance that the Company would be able to obtain additional working capital through the private placement of common stock or from any other source.

Going Concern

The accompanying financial statements have been prepared on a going concern basis of accounting, which contemplates continuity of operations, realization of assets and liabilities and commitments in the normal course of business. The accompanying financial statements do not reflect any adjustments that might result if the Company is unable to continue as a going concern. The Company does not generate significant revenue, and has negative cash flows from operations, which raise substantial doubt about the Company's ability to continue as a going concern. The ability of the Company to continue as a going concern and appropriateness of using the going concern basis is dependent upon, among other things, an additional cash infusion. The Company has obtained funds from its shareholders since its inception. It is management's plan to generate additional working capital from increasing sales from its desktop and mobile service offerings, and then continue to pursue its business plan and purposes.

4. BUSINESS ACQUISITIONS

Parscale Creative, Inc.

On August 1, 2017, the Company completed the acquisition of Parscale Creative, Inc., a Nevada corporation (“Parscale Creative”). As of that date, the Company’s wholly owned operating subsidiary, Parscale Digital, Inc., a Nevada corporation (“Parscale Digital”), merged with Parscale Creative, and the name of the combined subsidiary was changed to Parscale Digital. The total purchase price of \$7,945,000, was paid in the form of the issuance of ninety thousand (90,000) shares of the Company's Series D Convertible Preferred Stock, at a liquidation preference of one hundred dollars (\$100) per share, plus dividend payments based on 5% of adjusted revenue of Parscale Digital. Adjusted revenue is defined as total revenue, minus digital marketing media buys. Based on the growth of the Parscale Digital, the actual amount of the dividend payments is estimated to be in the range of \$850,000 and \$1,300,000, over 36 months, if we achieve 0.5% to 3% monthly adjusted revenue growth. The dividend payments are recorded as a reduction to additional paid in capital. For the period from acquisition, August 1, 2017 through December 31, 2017, we paid \$106,260 related to the Series D Convertible Preferred dividend, and during the six months ended June 30, 2018, we paid \$53,132. As of the date of closing,

Table of Contents

Brad Parscale, the 100% owner of Parscale Creative, was appointed to the Company's Board of Directors. The Company assumed net liabilities of \$535,000, related to this acquisition.

Under the purchase method of accounting, the transactions were valued for accounting purposes at \$7,945,000, which was the fair value of Parscale Creative at the time of acquisition. The assets and liabilities of Parscale Creative were recorded at their respective fair values as of the date of acquisition. The acquisition date estimated fair value of the consideration transferred and purchase price allocation consisted of the following:

| | |
|--|--------------|
| Cash | \$200,000 |
| Customer deposits and accrued expenses | (535,000) |
| Net tangible liabilities | \$(335,000) |

| | |
|------------------------|-------------|
| Non-compete agreements | \$280,000 |
| Brand name | 1,930,000 |
| Customer list | 2,090,000 |
| Goodwill | 4,720,000 |
| Deferred tax liability | (1,075,000) |
| Total purchase price | \$7,945,000 |

| | |
|--|-------------|
| Issuance of series D convertible preferred stock | \$7,610,000 |
| Net tangible liabilities | 335,000 |
| Total purchase price | \$7,945,000 |

WebTegrity, LLC

On November 15, 2017, the Company completed the acquisition of WebTegrity, LLC, a Texas limited liability company ("WebTegrity"). As of that date, the Company's operating subsidiary, Parscale Digital, Inc., a Nevada corporation, merged with WebTegrity and the name of the combined subsidiary remains unchanged as Parscale Digital. On April 16, 2018, we organized WebTegrity as a Nevada corporation, and split WebTegrity from Parscale Digital. The total purchase price of \$900,000, was paid in the form of the issuance of ten thousand (10,000) shares of the Company's Series E Convertible Preferred Stock, at a liquidation preference of one hundred dollars (\$100) per share.

Under the purchase method of accounting, the transactions were valued for accounting purposes at \$900,000, which was the fair value of WebTegrity at the time of acquisition. The assets and liabilities of WebTegrity were recorded at their respective fair values as of the date of acquisition. The acquisition date estimated fair value of the consideration transferred and purchase price allocation consisted of the following:

| | |
|----------------|-----------|
| Current assets | \$78,000 |
| Fixed assets | 30,000 |
| Liabilities | (48,000) |
| Net assets | 60,000 |
| Brand name | 130,000 |

| | |
|------------------------|-----------|
| Customer list | 280,000 |
| Goodwill | 530,000 |
| Deferred tax liability | (100,000) |
| Total purchase price | \$900,000 |

Issuance of Series E Convertible Preferred Stock \$900,000

Table of Contents

The above Parscale Creative and WebTegrity acquisitions are based on a preliminary purchase price allocation, and include identifiable intangible assets, which were based on their estimated fair values as of the acquisition date. The excess of purchase price over the estimated fair value of the net tangible and identifiable intangible assets acquired was recorded as goodwill. The allocation of the purchase price required management to make significant estimates in determining the fair values of assets acquired and liabilities assumed, especially with respect to identifiable intangible assets. These estimated fair values were based on information obtained from management of the acquired companies and historical experience and, with respect to the long-lived tangible and intangible assets, were made with the assistance of an independent valuation firm.

Parscale Media, LLC

On August 1, 2017, the Company entered into a purchase agreement with Brad Parscale, to purchase Parscale Media, LLC, a website hosting business, formed under the laws of Texas. Under the terms of the agreement, the Company agreed to pay Mr. Parscale \$1,000,000 in cash, upon closing the transaction, but in no event later than January 1, 2018.

On February 1, 2018, the Company entered into an amended purchase agreement which provided for the issuance of a promissory note with Mr. Parscale as consideration for the acquisition, under which the Company agreed to pay Mr. Parscale \$1,000,000 in twelve equal installments, and interest of 4% on the promissory note. For the six months ended June 30, 2018, the Company made total payments of \$255,450 on the promissory note, and included \$13,930 in interest expense.

| | |
|------------------------|-------------|
| Current assets | \$— |
| Brand name | 100,000 |
| Customer list | 400,000 |
| Goodwill | 625,000 |
| Deferred tax liability | (125,000) |
| Total purchase price | \$1,000,000 |

Pro forma results

The following tables set forth the unaudited pro forma results of the Company as if the acquisitions of Parscale Creative and WebTegrity had taken place on the first day of the period presented. These combined results are not necessarily indicative of the results that may have been achieved had the companies been combined as of the first day of the period presented.

| | Six months ended, | Six months ended, |
|---|----------------------|----------------------|
| | <u>June 30,</u> | <u>June 30,</u> |
| | <u>2018</u> | <u>2017</u> |
| Total revenues | \$5,474,359 | \$4,427,416 |
| Net income (loss) | (1,152,343) | 255,460 |
| Basic and diluted net earnings per common share | \$(0.01) | \$0.00 |

5.

INTANGIBLE ASSETS

Domain Name

On June 26, 2015, the Company purchased the rights to the domain “CLOUDCOMMERCE.COM”, from a private party at a purchase price of \$20,000, plus transaction costs of \$202, which is used as the main landing page for the Company. The total recorded cost of this domain of \$20,202 has been included in other assets on the balance sheet. As of June 30, 2018, we have determined that this domain has an indefinite useful life, and as such, is not included in depreciation and amortization expense. The Company will assess this intangible asset annually for impairment, in addition to it being classified with indefinite useful life.

Trademark

On September 22, 2015, the Company purchased the trademark rights of “CLOUDCOMMERCE”, from a private party at a purchase price of \$10,000. The total recorded cost of this trademark of \$10,000 has been included in other assets on the balance sheet. The trademark expires in 2020 and may be renewed for an additional 10 years. As of September 30,

15

Table of Contents

2015, we determined that this intangible asset has a definite useful life of 174 months, and as such, will be included in depreciation and amortization expense. For the six months ended June 30, 2018 and 2017, the Company included \$345 and \$345, respectively, in depreciation and amortization expense related to this trademark.

Non-Compete Agreements

On October 1, 2015, the Company acquired Indaba from three members of the limited liability company. At that time, we retained two of the members, who served as the Chief Executive Officer and Chief Technology Officer of Indaba. Both employees have non-compete agreements in place to protect the Company against the risk of either employee leaving Indaba to compete directly with us. We have calculated the value of those non-compete agreements at \$201,014, with a useful life of two years, which coincides with the term of the non-compete agreement. This amount was included in depreciation and amortization expense until September 30, 2017. For the six months ended June 30, 2018 and 2017, the Company included zero and \$50,254, respectively, in depreciation and amortization expense related to these non-compete agreements.

On August 1, 2017, the Company signed a merger agreement with Brad Parscale, in which Parscale Creative merged with and into Parscale Digital. The terms of the merger agreement include a non-compete agreement with Brad Parscale, for a period of three years. The Company has placed a value of this non-compete agreement at \$280,000, amortized over a period of 36 months. For the six months ended June 30, 2018, we have included \$46,667 in amortization expense related to this non-compete agreement. As of June 30, 2018, the balance on this intangible asset was \$194,444.

Customer List

On October 1, 2015, the Company acquired Indaba, and have calculated the value of the customer list at \$447,171, with a useful life of 3 years. This amount was to be included in depreciation and amortization expense until September 30, 2018. During the six months ended December 31, 2017, we determined that the Customer List intangible asset was impaired. Therefore, we have written off the remaining balance at December 31, 2017, totaling \$111,793. As of June 30, 2018 the balance is zero.

On August 1, 2017, the Company acquired Parscale Creative, and have calculated the value of the customer list at \$2,090,000, with a useful life of 3 years. For the six months ended June 30, 2018, we included \$339,972 in depreciation and amortization expense related to the customer list, and as of June 30, 2018, the remaining balance of this intangible asset was \$1,381,712.

On November 15, 2017, the Company acquired WebTegrity, and have calculated the value of the customer list at \$280,000, with a useful life of 3 years. For the six months ended June 30, 2018, we included \$44,815 in depreciation and amortization expense related to the customer list, and as of June 30, 2018, the remaining balance of this intangible asset was \$200,497.

On February 1, 2018, the Company acquired Parscale Media, and have calculated the value of the customer list at \$400,000, with a useful life of 3 years. For the six months ended June 30, 2018, we included \$55,556 in depreciation and amortization expense related to the customer list, and as of June 30, 2018, the remaining balance of this intangible asset was \$344,444.

Brand Name

On August 1, 2017, the Company acquired Parscale Creative, and have calculated the value of the brand name at \$1,930,000, which is included in other assets on the balance sheet. As of June 30, 2018, we have determined that this

brand name has an indefinite useful life, and as such, is not included in depreciation and amortization expense. The Company will assess this intangible asset annually for impairment, in addition to it being classified with an indefinite useful life.

On November 15, 2017, the Company acquired WebTegrity, and have calculated the value of the brand name at \$130,000, which is included in other assets on the balance sheet. As of June 30, 2018, we have determined that this brand name has an indefinite useful life, and as such, is not included in depreciation and amortization expense. The Company will assess this intangible asset annually for impairment, in addition to it being classified with an indefinite useful life.

On February 1, 2018, the Company acquired Parscale Media, and have calculated the value of the brand name at \$100,000, which is included in other assets on the balance sheet. As of June 30, 2018, we have determined that this brand name has an indefinite useful life, and as such, is not included in depreciation and amortization expense. The Company will assess this intangible asset annually for impairment, in addition to it being classified with an indefinite useful life.

Goodwill

On August 1, 2017, the Company acquired Indaba, and have calculated the value of the goodwill at \$1,128,003, which was included in other assets on the balance sheet at June 30, 2017. During the six months ended December 31, 2017, we

Table of Contents

determined that the goodwill related to the Indaba acquisition was impaired. Therefore, all remaining goodwill was written off. The amount of the write off was \$1,128,003.

On August 1, 2017, the Company acquired Parscale Creative, and have calculated the value of the goodwill at \$4,720,000, which is included in other assets on the balance sheet. The Company will assess this intangible asset for impairment, if an event occurs that may effect the fair value, or at least annually.

On November 15, 2017, the Company acquired WebTegrity, and have calculated the value of the goodwill at \$530,000, which is included in other assets on the balance sheet. The Company will assess this intangible asset for impairment, if an event occurs that may effect the fair value, or at least annually.

On February 1, 2018, the Company acquired Parscale Media, and have calculated the value of the goodwill at \$625,000, which is included in other assets on the balance sheet. The Company will assess this intangible asset for impairment, if an event occurs that may effect the fair value, or at least annually.

The Company's intangible assets consist of the following:

| | June 30, 2018 | | | December 31, 2017 | | |
|---------------------------|---------------|--------------------------|------------|-------------------|--------------------------|-----------|
| | Gross | Accumulated Amortization | Net | Gross | Accumulated Amortization | Net |
| Customer list | 2,770,000 | (843,346) | 1,926,654 | 2,370,000 | (403,003) | 1,966,997 |
| Non-compete agreement | 280,000 | (85,556) | 194,444 | 280,000 | (38,889) | 241,111 |
| Domain name and trademark | 30,201 | (1,896) | 28,305 | 30,201 | (1,552) | 28,649 |
| Brand name | 2,160,000 | — | 2,160,000 | 2,060,000 | — | 2,060,000 |
| Goodwill | 5,875,000 | — | 5,875,000 | 5,250,000 | — | 5,250,000 |
| Total | 11,115,201 | (930,798) | 10,184,403 | 9,990,201 | (443,444) | 9,546,757 |

Total amortization expense charged to operations for the six months ended June 30, 2018 and 2017 was \$487,354 and \$125,127, respectively. The following table of remaining amortization of finite life intangible assets, for the years ended December 31, includes the intangible assets acquired, in addition to the CloudCommerce trademark:

| | |
|---------------------|-------------|
| 2018 | \$488,253 |
| 2019 | 976,506 |
| 2020 | 646,953 |
| 2021 | 11,801 |
| 2022 and thereafter | 5,690 |
| Total | \$2,129,203 |

6. CREDIT FACILITIES

Secured Borrowing

On November 30, 2016, Indaba entered into a 12 month agreement with a third party to sell the rights to amounts due from our customers, in exchange for a borrowing facility in amounts up to a total of \$400,000. The agreement was amended on March 23, 2017, which increased the allowable borrowing amount by \$100,000, to a maximum of \$500,000. On November 30, 2017, the agreement auto renewed for another twelve months. The proceeds from the facility are determined by the amounts we invoice our customers. The Company evaluated this facility in accordance

with ASC 860, classifying it

17

Table of Contents

as a secured borrowing arrangement. As such, we record the amounts due from customers in accounts receivable and the amount due to the third party as a liability, presented as a “line of credit” on the Balance Sheet. The principal borrowed through this facility is secured by the accounts receivable balances, in addition to the other assets of the Company. During the term of this facility, the third party lender has a first priority security interest in the Company, and therefore, we will require such third party lender’s written consent to obligate the Company further or pledge our assets against additional borrowing facilities. Because of this position, it may be difficult for the Company to secure additional secured borrowing facilities. The cost of this secured borrowing facility is 0.05% of the daily balance. During the six months ended June 30, 2018 and 2017, the Company included \$15,079 and \$31,161, respectively, in interest expense, related to this secured borrowing facility, and as of June 30, 2018 and December 31, 2017, the outstanding balances were \$101,326 and \$296,631, respectively.

On October 19, 2017, Parscale Digital entered into a 12 month agreement with a third party to sell the rights to amounts due from our customers, in exchange for a borrowing facility in amounts up to a total of \$500,000. The agreement was amended on April 12, 2018, which increased the allowable borrowing amount by \$250,000, to a maximum of \$750,000. The proceeds from the facility are determined by the amounts we invoice our customers. The Company evaluated this facility in accordance with ASC 860, classifying it as a secured borrowing arrangement. As such, we record the amounts due from customers in accounts receivable and the amount due to the third party as a liability, presented as a “line of credit” on the Balance Sheet. The principal borrowed through this facility is secured by the accounts receivable balances, in addition to the other assets of the Company. During the term of this facility, the third party lender has a first priority security interest in the Company, and will, therefore, we will require such third party lender’s written consent to obligate the Company further or pledge our assets against additional borrowing facilities. Because of this position, it may be difficult for the Company to secure additional secured borrowing facilities. The cost of this secured borrowing facility is 0.05% of the daily balance. During the six months ended June 30, 2018 and 2017, the Company included \$16,712 and zero, respectively, in interest expense, related to this secured borrowing facility, and as of June 30, 2018 and December 31, 2017, the outstanding balances were \$382,847 and \$178,837, respectively.

7. CONVERTIBLE NOTES PAYABLE

During the quarter ended December 31, 2015, the Company signed an addenda to each of its outstanding convertible notes, fixing the conversion price at \$0.004. Before the addenda, the conversion price for each of the notes was tied to the trading price of the Company’s common stock. Because of that fluctuation, the Company was required to report derivative gains and losses each quarter, which was included in earnings, and an overall derivative liability balance on the balance sheet. Since the addenda, the Company has eliminated the derivative liability balance on the balance sheet and discontinued the gain/loss reporting on the income statement.

On March 25, 2013, the Company issued a convertible promissory note (the “March 2013 Note”) in the amount of up to \$100,000, at which time an initial advance of \$50,000 was received to cover operational expenses. The lender, a related party, advanced an additional \$20,000 on April 16, 2013, \$15,000 on May 1, 2013 and \$15,000 on May 16, 2013, for a total draw of \$100,000. The terms of the March 2013 Note, as amended, allow the lender to convert all or part of the outstanding balance plus accrued interest, at any time after the effective date, at a conversion price of \$0.004 per share. The March 2013 Note bears interest at a rate of 10% per year and matures on March 25, 2018. The Company is working with the lender to extend the maturity date. On May 23, 2014, the lender converted \$17,000 of the outstanding balance and accrued interest of \$1,975 into 4,743,699 shares of common stock. On October 14, 2014, the lender converted \$17,000 of the outstanding balance and accrued interest of \$2,645 into 4,911,370 shares of common stock. On April 17, 2018, the lender converted \$16,000 of the outstanding balance and accrued interest of \$8,106 into 6,026,301 shares of common stock. The balance of the March 2013 Note, as of June 30, 2018 was \$75,856, which includes \$25,856 of accrued interest.

On April 20, 2018, the Company issued a convertible promissory note (the “April 2018 Note”) in the amount of up to \$200,000, at which time an initial advance of \$200,000 was received to cover operational expenses. The terms of the April 2018 Note, as amended, allow the lender, a related party, to convert all or part of the outstanding balance plus accrued interest, at any time after the effective date, at a conversion price of \$0.01 per share. The April 2018 Note bears interest at a rate of 5% per year and matures on April 20, 2021. The balance of the April 2018 Note, as of June 30, 2018 was \$201,945, which includes \$1,945 of accrued interest.

8. NOTES PAYABLE

On July 31, 2017, the Company signed an exchange agreement with the holder of our notes, which exchanged ten convertible notes, totaling \$1,485,914, for 14,425 shares of Series C Preferred stock. Each share of Series C Preferred stock has a face value of \$100 and is convertible into common stock at a price of \$0.01 per share. At the time of the exchange, all accrued interest was forgiven. The following notes were converted:

Table of Contents

(a) On January 12, 2016, the Company borrowed \$100,000 from Bountiful Capital, LLC to cover operating costs. The loan was offered interest free on a short term basis, and was due February 12, 2016. On July 31, 2017, the principal balance of \$100,000 was exchanged for Series C Preferred stock, leaving a balance of zero as of July 31, 2017. The other notes exchanged with Bountiful Capital, LLC, are noted below.

(b) On April 18, 2016, the Company issued a promissory note (the “April 2016 Note”) in the amount of up to \$500,000, at which time an initial advance of \$35,500 was received to cover operational expenses. The lender advanced an additional \$41,000 on May 2, 2016, \$35,000 on May 17, 2016, \$160,000 on May 19, 2016, \$34,000 on June 1, 2016, \$21,000 on June 21, 2016, \$33,500 on June 30, 2016, \$10,000 on July 15, 2016, \$33,000 on July 29, 2016, \$35,500 on August 16, 2016, \$28,000 on August 31, 2016, \$33,500 on September 14, 2016, for a total draw of \$500,000. The April 2016 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 60 months from the effective date of each tranche. On July 31, 2017, the principal balance of \$500,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(c) On October 3, 2016, the Company issued a promissory note (the “October 2016 Note”) in the amount of up to \$500,000, at which time an initial advance of \$36,000 was received to cover operational expenses. The lender advanced an additional \$48,000 on October 17, 2016, \$34,000 on October 31, 2016, \$27,000 on November 15, 2016, \$34,000 on November 30, 2016, \$28,500 on December 16, 2016, \$21,000 on January 3, 2017, \$50,000 on January 17, 2017, \$29,000 on January 31, 2017, \$15,000 on February 2, 2017, \$30,000 on February 16, 2017, \$29,000 on March 1, 2017, \$28,000 on March 16, 2017, \$46,500 on April 3, 2017, \$23,500 on April 17, 2017, and \$20,500 on May 2, 2017, for a total draw of \$500,000. The October 2016 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 60 months from the effective date of each tranche. On July 31, 2017, the principal balance of \$500,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(d) On May 16, 2017, the Company issued a promissory note (the “May 16, 2017 Note”) in the amount of \$38,000, at which time the entire balance of \$38,000 was received to cover operational expenses. The May 16, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$38,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(e) On May 30, 2017, the Company issued a promissory note (the “May 30, 2017 Note”) in the amount of \$46,000, at which time the entire balance of \$46,000 was received to cover operational expenses. The May 30, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$46,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(f) On June 14, 2017, the Company issued a promissory note (the “June 14, 2017 Note”) in the amount of \$26,000, at which time the entire balance of \$26,000 was received to cover operational expenses. The June 14, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$26,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(g) On June 29, 2017, the Company issued a promissory note (the “June 29, 2017 Note”) in the amount of \$23,500, at which time the entire balance of \$23,500 was received to cover operational expenses. The June 29, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$23,500 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(h) On July 10, 2017, the Company issued a promissory note (the “July 10, 2017 Note”) in the amount of \$105,000, at which time the entire balance of \$105,000 was received to cover operational expenses. The July 10, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$105,000 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(i) On July 14, 2017, the Company issued a promissory note (the “July 14, 2017 Note”) in the amount of \$50,500, at which time the entire balance of \$50,500 was received to cover operational expenses. The July 14, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$50,500 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

(j) On July 30, 2017, the Company issued a promissory note (the “July 30, 2017 Note”) in the amount of \$53,500, at which time the entire balance of \$53,500 was received to cover operational expenses. The July 30, 2017 Note bears interest

Table of Contents

at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. On July 31, 2017, the principal balance of \$53,500 was exchanged for Series C Preferred stock, and all accrued interest was forgiven, leaving a balance of zero as of July 31, 2017.

Subsequent to July 31, 2017, the Company entered into the following new notes payable:

On August 3, 2017, the Company issued a promissory note (the “August 3, 2017 Note”) in the amount of \$25,000, at which time the entire balance of \$25,000 was received to cover operational expenses. The August 3, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the August 3, 2017 Note, as of June 30, 2018 is \$26,332, which includes \$1,332 of accrued interest.

On August 15, 2017, the Company issued a promissory note (the “August 15, 2017 Note”) in the amount of \$34,000, at which time the entire balance of \$34,000 was received to cover operational expenses. The August 15, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the August 15, 2017 Note, as of June 30, 2018 is \$35,695, which includes \$1,695 of accrued interest.

On August 28, 2017, the Company issued a promissory note (the “August 28, 2017 Note”) in the amount of \$92,000, at which time the entire balance of \$92,000 was received to cover operational expenses. The August 28, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the August 28, 2017 Note, as of June 30, 2018 is \$96,272, which includes \$4,272 of accrued interest.

On September 28, 2017, the Company issued a promissory note (the “September 28, 2017 Note”) in the amount of \$63,600, at which time the entire balance of \$63,600 was received to cover operational expenses. The September 28, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the September 28, 2017 Note, as of June 30, 2018 is \$66,013, which includes \$2,413 of accrued interest.

On October 11, 2017, the Company issued a promissory note (the “October 11, 2017 Note”) in the amount of \$103,500, at which time the entire balance of \$103,500 was received to cover operational expenses. The October 11, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the October 11, 2017 Note, as of June 30, 2018 is \$107,215, which includes \$3,715 of accrued interest.

On October 27, 2017, the Company issued a promissory note (the “October 27, 2017 Note”) in the amount of \$106,000, at which time the entire balance of \$106,000 was received to cover operational expenses. The October 27, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the October 27, 2017 Note, as of June 30, 2018 is \$109,572, which includes \$3,572 of accrued interest.

On November 15, 2017, the Company issued a promissory note (the “November 15, 2017 Note”) in the amount of \$62,000, at which time the entire balance of \$62,000 was received to cover operational expenses. The November 15, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the November 15, 2017 Note, as of June 30, 2018 is \$63,928, which includes \$1,928 of accrued interest.

On November 27, 2017, the Company issued a promissory note (the “November 27, 2017 Note”) in the amount of \$106,000, at which time the entire balance of \$106,000 was received to cover operational expenses. The November 27, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the November 27, 2017 Note, as of June 30, 2018 is \$109,122, which includes \$3,122 of accrued interest.

On November 30, 2017, the Company issued a promissory note (the “November 30, 2017 Note”) in the amount of \$30,000, at which time the entire balance of \$30,000 was received to cover operational expenses. The November 30, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the November 30, 2017 Note, as of June 30, 2018 is \$30,871, which includes \$871 of accrued interest.

On December 19, 2017, the Company issued a promissory note (the “December 19, 2017 Note”) in the amount of \$42,000, at which time the entire balance of \$42,000 was received to cover operational expenses. The December 19, 2017 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the December 19, 2017 Note, as of June 30, 2018 is \$43,110, which includes \$1,110 of accrued interest.

On January 3, 2018, the Company issued a promissory note (the “January 3, 2018 Note”) in the amount of \$49,000, at which time the entire balance of \$49,000 was received to cover operational expenses. The January 3, 2018 Note bears

Table of Contents

interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the January 3, 2018 Note, as of June 30, 2018 is \$50,195, which includes \$1,195 of accrued interest.

On January 30, 2018, the Company issued a promissory note (the "January 30, 2018 Note") in the amount of \$72,000, at which time the entire balance of \$72,000 was received to cover operational expenses. The January 30, 2018 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the January 30, 2018 Note, as of June 30, 2018 is \$73,489, which includes \$1,489 of accrued interest.

On February 1, 2018, the Company entered into an amended purchase agreement and promissory note with Mr. Parscale, which facilitated the closing of the Parscale Media transaction and established a revised payment arrangement, under which the Company agreed to pay Mr. Parscale \$1,000,000 in twelve equal installments, which includes 4% interest. For the six months ended June 30, 2018, the Company made total payments of \$255,450 on the promissory note, which includes \$9,181 of interest expense. For the six months ended June 30, 2018, we included \$13,930 in interest expense related to this liability.

On February 2, 2018, the Company issued a promissory note (the "February 2, 2018 Note") in the amount of \$85,000, at which time the entire balance of \$85,000 was received to cover operational expenses. The February 2, 2018 Note bears interest at a rate of 5% per year and is payable upon demand, but in no event later than 36 months from the effective date. The balance of the February 2, 2018 Note, as of June 30, 2018 is \$86,723, which includes \$1,723 of accrued interest.

As of June 30, 2018 and December 31, 2017, the notes payable due to related parties totaled \$1,657,020 and \$670,819, respectively.

9. CAPITAL STOCK

At June 30, 2018 the Company's authorized stock consists of 2,000,000,000 shares of common stock, par value \$0.001 per share. The Company is also authorized to issue 5,000,000 shares of preferred stock, par value of \$0.001 per share. The rights, preferences and privileges of the holders of the preferred stock will be determined by the Board of Directors prior to issuance of such shares. The conversion of certain outstanding preferred stock could have a significant impact on our common stockholders.

Series A Preferred

The Company has designated 10,000 shares of its preferred stock as Series A Preferred Stock. Each share of Series A Preferred Stock is convertible into 10,000 shares of the Company's common stock. The holders of outstanding shares of Series A Preferred Stock shall be entitled to receive dividends, payable quarterly, out of any assets of the Corporation legally available therefor, at the rate of \$8 per share per annum, payable in preference and priority to any payment of any dividend on the common stock. As of June 30, 2018, the Company has 10,000 shares of Series A Preferred Stock outstanding.

Series B Preferred

The Company has designated 25,000 shares of its preferred stock as Series B Preferred Stock. Each share of Series B Preferred Stock shall have a stated value of \$100. The Series B Preferred Stock is convertible into shares of fully paid and non-assessable shares of the Company's common stock by dividing the stated value by a conversion price of

\$0.004 per share. Series B Preferred Stock shall not be entitled to vote, as a separate class or otherwise, on any matter presented to the stockholders of the Company for their action or consideration at any meeting of stockholders of the Company. As of June 30, 2018, the Company has 18,025 shares of Series B Preferred Stock outstanding.

Series C Preferred

The Company has designated 25,000 shares of its preferred stock as Series C Preferred Stock. Each share of Series C Preferred Stock shall have a stated value of \$100. The Series C Preferred Stock is convertible into shares of fully paid and non-assessable shares of the Company's common stock by dividing the stated value by a conversion price of \$0.01 per share. Series C Preferred Stock shall not be entitled to vote, as a separate class or otherwise, on any matter presented to the stockholders of the Company for their action or consideration at any meeting of stockholders of the Company. As of June 30, 2018, the Company has 14,425 shares of Series C Preferred Stock outstanding.

Series D Preferred

The Company has designated 90,000 shares of its preferred stock as Series D Preferred Stock. Each share of Series D Preferred Stock shall have a stated value of \$100. The Series D Preferred Stock is convertible into common stock at a ratio of 2,500 shares of common stock per share of preferred stock, and pays a quarterly dividend, calculated as $(1/90,000) \times (5\% \text{ of the Adjusted Gross Revenue})$ of the Company's subsidiary Parscale Digital. Adjusted Gross Revenue shall mean the top line gross revenue of Parscale Digital, as calculated under GAAP (generally accepted accounting principles) less any reselling revenue attributed to third party advertising products or service, such as, but not limited to, search engine

Table of Contents

keyword campaign fees, social media campaign fees, radio or television advertising fees, and the like. Series D Preferred Stock shall not be entitled to vote, as a separate class or otherwise, on any matter presented to the stockholders of the Company for their action or consideration at any meeting of stockholders of the Company. As of June 30, 2018, the Company has 90,000 shares of Series D Preferred Stock outstanding.

Series E Preferred

The Company has designated 10,000 shares of its preferred stock as Series E Preferred Stock. Each share of Series E Preferred Stock shall have a stated value of \$100. The Series E Preferred Stock is convertible into shares of fully paid and non-assessable shares of the Company's common stock by dividing the stated value by a conversion price of \$0.05 per share. Series E Preferred Stock shall not be entitled to vote, as a separate class or otherwise, on any matter presented to the stockholders of the Company for their action or consideration at any meeting of stockholders of the Company. As of June 30, 2018, the Company has 10,000 shares of Series E Preferred Stock outstanding.

10. STOCK OPTIONS AND WARRANTS

Stock Options

On July 10, 2003, the Company adopted the Warp 9, Inc. Stock Option Plan for directors, executive officers, and employees of and key consultants to the Company. Pursuant to the now terminated plan, the Company could issue 5,000,000 shares of common stock. The plan was administered by the Company's Board of Directors, and options granted under the plan could be either incentive options or nonqualified options. Each option was exercisable in full or in installment and at such time as designated by the Board. Notwithstanding any other provision of the plan or of any option agreement, each option expired on the date specified in the option agreement, which date was to be no later than the tenth anniversary of the date on which the option was granted (fifth anniversary in the case of an incentive option granted to a greater-than-10% stockholder). The purchase price per share of the common stock under each incentive option was to be no less than the fair market value of the common stock on the date the option was granted (110% of the fair market value in the case of a greater-than-10% stockholder). The purchase price per share of the common stock under each nonqualified option was to be specified by the Board at the time the option is granted, and could be less than, equal to or greater than the fair market value of the shares of common stock on the date such nonqualified option was granted, but was to be no less than the par value of shares of common stock. The plan provided specific language as to the termination of options granted thereunder.

On August 1, 2017, we granted non-qualified stock options to purchase up to 10,000,000 shares of our common stock to Jill Giles, at a price of \$0.01 per share. The stock options vest equally over a period of 36 months and expire August 1, 2022.

On September 18, 2017, we granted non-qualified stock options to purchase up to 1,800,000 shares of our common stock to three key employees, at a price of \$0.05 per share. The stock options vest equally over a period of 36 months and expire September 18, 2022.

On January 3, 2018, we granted non-qualified stock options to purchase up to 20,000,000 shares of our common stock to three key employees, at a price of \$0.04 per share. The stock options vest equally over a period of 36 months and expire January 3, 2023.

The Company used the historical industry index to calculate volatility, since the Company's stock history did not represent the expected future volatility of the Company's common stock. The fair value of options granted during the six months ended June 30, 2018 and year ended December 31, 2017, were determined using the Black Scholes method with the following assumptions:

| | Six months ended | | Year ended | |
|---------------------------------------|------------------------|---|----------------------|---|
| | June 30, 2018 | | December 31, 2017 | |
| Risk free interest rate | 5.00 | % | 5.00 | % |
| Stock volatility factor | 397 | % | 397 | % |
| Weighted average expected option life | 5 years | | 5 years | |
| Expected dividend yield | none | | none | |

Table of Contents

A summary of the Company's stock option activity and related information follows:

| | Six Months ended June 30, 2018 | | Six Months ended June 30, 2017 | |
|---|-----------------------------------|--|-----------------------------------|--|
| | Options | Weighted average exercise price | Options | Weighted average exercise price |
| Outstanding -beginning of period | 134,800,000 | \$0.013 | 123,000,000 | \$ 0.013 |
| Granted | 20,000,000 | \$0.040 | — | \$ — |
| Exercised | — | \$— | — | \$— |
| Forfeited | — | \$— | — | \$— |
| Outstanding - end of period | 154,800,000 | \$0.017 | 123,000,000 | \$ 0.013 |
| Exercisable at the end of the period | 125,738,995 | \$0.013 | 94,095,890 | \$ 0.012 |
| Weighted average fair value of options granted during the year | | \$800,000 | | \$— |

As of June 30, 2018 and December 31, 2017, the intrinsic value of the stock options was approximately \$1,783,750 and \$3,632,450, respectively. Stock option expense for the six months ended June 30, 2018 and 2017 was \$285,976 and \$248,937, respectively.

The Black Scholes option valuation model was developed for use in estimating the fair value of traded options, which do not have vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The weighted average remaining contractual life of options outstanding, as of June 30, 2018 was as follows:

| Exercise prices | Number of options outstanding | Weighted Average remaining contractual life (years) |
|-----------------|-------------------------------------|---|
| \$0.050 | 1,800,000 | 4.22 |
| \$0.040 | 20,000,000 | 4.52 |
| \$0.015 | 35,000,000 | 4.16 |
| \$0.013 | 60,000,000 | 3.60 |
| \$0.013 | 15,000,000 | 3.72 |
| \$0.010 | 10,000,000 | 4.09 |
| \$0.005 | 12,500,000 | 1.12 |
| \$0.004 | 500,000 | 3.29 |
| | 154,800,000 | |

Warrants

During the six months ended June 30, 2018 and 2017, the Company issued no warrants for services, and no warrants were outstanding.

11. RELATED PARTIES

Bountiful Capital, LLC, loaned the Company \$100,000 on January 12, 2016, \$500,000 through multiple fundings on the April 2016 Note, \$500,000 through multiple fundings on the October 2016 Note, \$38,000 on May 16, 2017, \$46,000 on May 30, 2017, \$26,000 on June 14, 2017, \$23,500 on June 29, 2017, \$105,000 on July 10, 2017, \$50,500 on July 14, 2017, \$53,500 on July 30, 2017, \$25,000 on August 3, 2017, \$34,000 on August 16, 2017, \$92,000 on August 28, 2017, \$63,600 on September 28, 2017, \$103,500 on October 11, 2017, \$106,000 on October 27, 2017, \$62,000 on November 15, 2017, \$106,000 on November 27, 2017, \$30,000 on November 30, 2017, \$42,000 on December 19, 2017, \$49,000 on January 3, 2018, \$72,000 on January 30, 2018 and \$85,000 on February 2, 2018, as unsecured promissory notes. The terms of the notes include interest of 5% and are due and payable upon demand, but in no case later than 36 months after the effective date. On July 31,

Table of Contents

2017, notes payable amounting to \$1,442,500 and accrued interest of \$43,414 were converted into 14,425 shares of Series C preferred stock. At June 30, 2018, notes payable and accrued interest amount to \$898,539. The Company's chief financial officer, Greg Boden, also serves as the president of Bountiful Capital, LLC.

Brad Parscale has served on the board of directors of the Company since the acquisition of Parscale Creative on August 1, 2017. Mr. Parscale is also the owner of Parscale Strategy, LLC ("Parscale Strategy"), the largest customer of Parscale Digital. During the six months ended June 30, 2018, the Company earned \$2,008,317 in revenue from providing services to Parscale Strategy, and as of June 30, 2018, Parscale Strategy had an outstanding accounts receivable of \$148,024.

On August 1, 2017, Parscale Digital signed a lease with Giles-Parscale, Inc., a related party, to provide a workplace for the employees of Parscale Digital. Giles-Parscale, Inc., is wholly owned by Jill Giles, an employee of the Company. Details on this lease are included in Note 13.

On August 1, 2017, Parscale Digital signed a lease with Parscale Strategy for computer equipment and office furniture. Parscale Strategy is wholly owned by Brad Parscale, who serves on the CloudCommerce board of directors. Details of this lease are included in Note 13.

On February 1, 2018, the Company entered into an amended purchase agreement and promissory note with Mr. Parscale, which facilitated the closing of the Parscale Media transaction and established a revised payment arrangement, under which the Company agreed to pay Mr. Parscale \$1,000,000 in twelve equal installments, which includes 4% interest. For the six months ended June 30, 2018, the Company made total payments of \$255,450 on the promissory note, which includes \$9,181 of interest expense.

On April 28, 2018, Data Propria entered into an agreement to lease approximately 2,073 square feet of office space located at 311 Sixth Street, San Antonio, TX 78215, for a period of twelve months, commencing May 1, 2018, at a cost of \$4,000 per month, plus a pro rata share of building maintenance expenses. This lease was signed with a related party, Jill Giles, an employee of the Company.

12. CONCENTRATIONS

For the six months ended June 30, 2018 and 2017, the Company had one and three major customers who represented approximately 37% and 58% of total revenue. At June 30, 2018 and December 31, 2017, accounts receivable from two and four customers, represented approximately 19% and 56% of total accounts receivable, respectively. The customers comprising the concentrations within the accounts receivable are not the same customers that comprise the concentrations with the revenues discussed above.

13. COMMITMENTS AND CONTINGENCIES

Operating Leases

As a result of the WebTegrity acquisition, we assumed a lease for office space used by the WebTegrity employees, at 14603 Huebner Road, Suite 3402, San Antonio, TX 78230. The lease was executed on March 20, 2017 for a period of 36 months, commencing March 20, 2017, at a rate of \$2,750 per month.

On August 1, 2017, Parscale Digital signed a lease agreement with Giles-Parscale, Inc., a related party, which commenced on August 1, 2017, for approximately 8,290 square feet, at 321 Sixth Street, San Antonio, TX 78215, for \$9,800 per month, plus a pro rata share of the common building expenses. The lease expires on July 31, 2022.

On April 15, 2016, the CloudCommerce signed a lease for approximately 1,800 square feet of office space at 1933 Cliff Dr., Suite 1, Santa Barbara, California 93109 for approximately \$3,000 per month, on a month-to-month basis which lease commenced on March 1, 2016 and concluded February 15, 2018. On October 24, 2017, we executed a lease agreement for the same space, commencing March 1, 2018 for a period of 36 months, at a rate of \$2,795 per month, plus a pro rata share of the common area maintenance.

On December 10, 2012, Indaba signed a lease, which commenced January 16, 2013 for approximately 3,300 square feet at 2854 Larimer Street, Denver, CO 80205, for approximately \$3,500 per month. The original lease term expired February 28, 2016, but was extended until February 28, 2017, at a rate of \$5,800 per month. This lease was further extended until February 28, 2018, at a rate of \$5,850 per month. We did not renew this lease and moved out of the space by February 28, 2018. On February 12, 2018, we executed a lease agreement for office space at 1415 Park Avenue West, Denver, CO 80205, expiring August 14, 2018, at a cost of \$800 per month. This lease was cancelled June 30, 2018.

Table of Contents

The following is a schedule, by years, of future minimum lease payments required under the operating leases.

| Years Ending December 31, | Amount |
|------------------------------------|------------|
| 2018 | \$ 117,667 |
| 2019 | 204,334 |
| 2020 | 160,854 |
| 2021 | 125,984 |
| 2022 | 68,600 |

Total operating lease expense for the six months ended June 30, 2018 and 2017 was \$118,957 and \$52,801, respectively. The Company is also required to pay its pro rata share of taxes, building maintenance costs, and insurance in according to the lease agreement.

On May 21, 2014, the Company entered into a settlement agreement with the landlord of our previous location, to make monthly payments on past due rent totaling \$227,052. Under the terms of the agreement, the Company will make monthly payments of \$350 on a reduced balance of \$40,250. Upon payment of \$40,250, the Company will record a gain on extinguishment of debt of \$186,802. As of June 30, 2018, the Company recorded the outstanding balance under this settlement agreement as a long-term accrued expense, with the current portion of the debt recorded in accrued expenses. As of June 30, 2018 and December 31, 2017, the Company owed \$23,100 and \$25,200 on the outstanding reduced payment terms, respectively.

Capital Lease

On August 1, 2017, Parscale Digital signed a lease agreement with Parscale Strategy, a related party, for the use of office equipment and furniture. The lease provides for a term of thirty-six (36) months, at a monthly payment of \$3,000, and an option to purchase all items at the end of the lease for one dollar. We have evaluated this lease in accordance with ASC 840-30 and determined that it meets the definition of a capital lease.

The following is a schedule of the net book value of the capital lease.

| Assets | June 30, 2018 | December 31, 2017 |
|---------------------------------------|------------------|----------------------|
| Leased equipment under capital lease, | \$ 100,097 | \$ 100,097 |
| less accumulated amortization | (22,761) | (13,023) |
| Net | \$ 77,336 | \$ 87,075 |

| Liabilities | June 30, 2018 | December 31, 2017 |
|--|------------------|----------------------|
| Obligations under capital lease (current) | \$ 32,382 | \$ 32,382 |
| Obligations under capital lease (noncurrent) | 37,804 | \$ 54,693 |
| Total | \$ 71,086 | \$ 87,075 |

The following is a schedule, by years, of future minimum lease payments required under the capital lease.

| Years ended December 31, | Lease Payments | Imputed Interest | Present Value of Payments |
|-----------------------------------|-------------------|---------------------|---------------------------------|
| 2018 | \$ 18,000 | \$(1,607) | \$ 16,393 |
| 2019 | 36,000 | (1,962) | 34,038 |
| 2020 | 21,000 | (345) | 20,655 |
| 2021 | — | — | — |
| 2022 | — | — | — |
| | \$ 75,000 | \$(3,914) | \$ 71,086 |

Table of Contents

The Company is required to pay its pro rata share of taxes, building maintenance costs, and insurance in accordance with the operating lease agreements of CloudCommerce, Parscale Digital, WebTegrity, Parscale Media, Giles Design Bureau and Data Propria.

Legal Matters

The Company may be involved in legal actions and claims arising in the ordinary course of business, from time to time, none of which at the time are considered to be material to the Company's business or financial condition.

14. SUPPLEMENTAL STATEMENT OF CASH FLOWS INFORMATION

During the six months ended June 30, 2018, there were the following non-cash financing activities:

-On February 1, 2018, the Company acquired Parscale Media for \$1,000,000 payable by a note over twelve months.

On April 17, 2018, a lender converted a portion of the March 2013 Note into common stock. The conversion included \$16,000 of principal, plus \$8,106 of interest, which was converted into 6,026,301 common shares.

During the six months ended June 30, 2017, there were no non-cash financing activities.

15. SUBSEQUENT EVENTS

Management has evaluated subsequent events according to ASC TOPIC 855 as of the date of the financial statements and has determined that there are no reportable events.

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

Cautionary Statements

The following Management's Discussion and Analysis should be read in conjunction with our financial statements and the related notes thereto included elsewhere herein. The Management's Discussion and Analysis contains forward-looking statements that involve risks and uncertainties, such as statements of our plans, objectives, expectations and intentions. Any statements that are not statements of historical fact are forward-looking statements. When used, the words "believe," "plan," "intend," "anticipate," "target," "estimate," "expect," and the like, and/or future-tense or conditional constructions ("will," "may," "could," "should," etc.), or similar expressions, identify certain of these forward-looking statements. These forward-looking statements are subject to risks and uncertainties that could cause actual results or events to differ materially from those expressed or implied by the forward-looking statements in this quarterly report. Our actual results and the timing of events could differ materially from those anticipated in these forward-looking statements as a result of several factors including, but not limited to, those noted under "Risk Factors" of the reports filed with the Securities and Exchange Commission. We do not undertake any obligation to update forward-looking statements to reflect events or circumstances occurring after the date of this quarterly report.

Overview

CloudCommerce, Inc. ("CloudCommerce," "we," "us," "our," or the "Company") is a leading provider of data driven solutions. We develop solutions that help our clients acquire, engage, and retain their customers by leveraging cutting edge digital strategies and technologies. We focus intently on using data analytics to drive the creation of great user

experiences and effective digital marketing campaigns. Whether it is creating omni-channel experiences, engaging a specific audience, or energizing voters in political campaigns, we believe data is the key to digital success. Our goal is to become the industry leader by always applying a “data first” strategy and acquiring other companies that can help us achieve this vision.

To better serve our customers and create value for our shareholders, we strategically acquire profitable cloud commerce solutions providers with strong management teams.

We believe our products and services allow our clients to lower costs and focus on promoting and marketing their brand, product line and website while leveraging the investments we have made in technology and infrastructure to operate a dynamic digital presence.

Data Analytics

To deliver the highest Return on Investment (“ROI”) for our customer’s digital marketing campaign, we utilize sophisticated data science to identify the correct universes to target relevant audiences. Our ability to understand and translate data drives every decision we make. By listening to and analyzing our customers’ data we are able to make informed decisions that positively impact our customers’ business. We leverage industry-best tools to aggregate and visualize data

Table of Contents

across multiple sources, and then our data and behavioral scientists segment and model that data to be deployed in targeted marketing campaigns. We have data analytics expertise in retail, wholesale, distribution, logistics, manufacturing, political, and several other industries.

Digital Marketing

We help our customers get their message out, educate their market and tell their story. We do so creatively and effectively by deploying powerful call-to-action digital campaigns with national reach, and boosting exposure and validation with coordinated advertising in print media. Our fully-developed marketing plans are founded on sound research methodologies, brand audits and exploration of the competitive landscape. Whether our customer is a challenger brand, a political candidate, or a well-known household name, our strategists are skillful at leveraging data and creating campaigns that move people to make decisions.

Branding and Creative Services

We approach branding from a “big picture” perspective, establishing a strong identity and then building on that to develop a comprehensive branding program that tells our customer’s story, articulates what sets our customer apart from their competitors and establishes our customer in their market.

Development and Managed Infrastructure Support

Commerce-focused, user-friendly digital websites and apps, elevates our customer’s marketing position and draw consumers to their products and services. Our platform-agnostic approach allows us to architect and build solutions that are the best fit for each customer. Once the digital properties are built, our experts will help manage and protect the website or app and provide the expertise needed to scale the infrastructure needed as our customer’s business grows.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations, including the discussion on liquidity and capital resources, are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, management re-evaluates its estimates and judgments, particularly those related to the determination of the estimated recoverable amounts of trade accounts receivable, impairment of long-lived assets, revenue recognition, and deferred tax assets. We believe the following critical accounting policies require more significant judgment and estimates used in the preparation of the financial statements.

Among the significant judgments made by management in the preparation of our financial statements are the following:

Revenue recognition

The Company recognizes income when the service is provided or when the product is delivered. We present service revenue, net of customer incentives. Most of the income is generated from professional services and site development fees. We provide online marketing services that we purchase from third parties. The gross revenue presented in our statement of operations is in accordance with ASC 605-45, and includes digital advertising revenue. We also offer

professional services such as development services. The fees for development services with multiple deliverables constitute a separate unit of accounting in accordance with ASC 605-25, which are recognized as the work is performed. Upfront fees for development services or other customer services are deferred until certain implementation or contractual milestones have been achieved. If we have performed work for our clients, but have not invoiced clients for that work, then we record the value of the work in either deferred revenue, as a negative liability balance, or as an asset in costs in excess of billings.

Accounts receivable

The Company extends credit to its customers who are located nationwide. Accounts receivable are customer obligations due under normal trade terms. The Company performs continuing credit evaluations of its customers' financial condition. Management reviews accounts receivable on a regular basis, based on contracted terms and how recently payments have been received to determine if any such amounts will potentially be uncollected. The Company includes any balances that are determined to be uncollectible in its allowance for doubtful accounts.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of a long-lived asset, management evaluates whether the estimated future undiscounted net cash flows from the asset are less than its carrying amount. If impairment is indicated, the long-lived asset would be written down to fair value. Fair value is determined by an evaluation of available price information at which assets could be bought or sold, including quoted market prices, if available, or the present value of the estimated future cash flows based on reasonable and supportable assumptions.

Table of Contents

Indefinite Lived Intangibles and Goodwill Assets

The Company accounts for business combinations under the acquisition method of accounting in accordance with ASC 805, "Business Combinations," where the total purchase price is allocated to the tangible and identified intangible assets acquired and liabilities assumed based on their estimated fair values. The purchase price is allocated using the information currently available, and may be adjusted, up to one year from acquisition date, after obtaining more information regarding, among other things, asset valuations, liabilities assumed and revisions to preliminary estimates. The purchase price in excess of the fair value of the tangible and identified intangible assets acquired less liabilities assumed is recognized as goodwill.

The Company tests for indefinite lived intangibles and goodwill impairment in the fourth quarter of each year and whenever events or circumstances indicate that the carrying amount of the asset exceeds its fair value and may not be recoverable. In accordance with its policies, the Company performed a qualitative assessment of indefinite lived intangibles and goodwill at December 31, 2017, and determined there was impairment of indefinite lived intangibles and goodwill from our Indaba acquisition. Accordingly, all intangible assets and goodwill related to the Indaba acquisition has been written off at that time, amounting to \$1,239,796.

Business Combinations

The Company allocates the fair value of purchase consideration to the tangible assets acquired, liabilities assumed and intangible assets acquired based on their estimated fair values. The excess of the fair value of purchase consideration over the fair values of these identifiable assets and liabilities is recorded as goodwill. Such valuations require management to make significant estimates and assumptions, especially with respect to intangible assets. Significant estimates in valuing certain intangible assets include, but are not limited to, future expected cash flows from acquired customer lists, acquired technology, and trade names from a market participant perspective, useful lives and discount rates. Management's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. During the measurement period, which is one year from the acquisition date, we may record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period, any subsequent adjustments are recorded to earnings.

Fair value of financial instruments

The Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities are carried at cost, which approximates their fair value, due to the relatively short maturity of these instruments. As of June 30, 2018 and December 31, 2017, the Company's notes payable have stated borrowing rates that are consistent with those currently available to the Company and, accordingly, the Company believes the carrying value of these debt instruments approximates their fair value.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 established a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). These tiers include:

- Level 1, defined as observable inputs such as quoted prices for identical instruments in active markets;
- Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable such as quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active; and

Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions, such as valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Recent Accounting Pronouncements

There were various updates recently issued, most of which represented technical corrections to the accounting literature or application to specific industries and are not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

Table of Contents

Results of Operations for the Three Months Ended June 30, 2018, compared to the Three Months Ended June 30, 2017.

REVENUE

Total revenue for the three months ended June 30, 2018 increased by \$1,873,833 to \$2,597,650, compared to \$723,817 for the three months ended June 30, 2017. The increase was primarily due to revenues generated from the recently acquired Parscale Creative and WebTegrity, and the addition of the newly formed Data Propria, partially offset by a reduction in revenue at Indaba.

SALARIES AND OUTSIDE SERVICES

Salaries and outside services for the three months ended June 30, 2018 increased by \$677,149 to \$1,462,011, compared to \$784,862 for the three months ended June 30, 2017. The increase was primarily due to expenses related to the recently acquired Parscale Creative and WebTegrity, and newly established Data Propria, due to additional employees added to payroll expense.

SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES

Selling, general, and administrative (“SG&A”) expenses for the three months ended June 30, 2018 increased by \$919,194 to \$1,128,626, compared to \$209,432 for the three months ended June 30, 2017. The increase was primarily due to operating expenses related to the recently acquired Parscale Creative and WebTegrity, and the increase in costs to maintain the additional offices in San Antonio.

STOCK BASED COMPENSATION

Stock based compensation expenses for the three months ended June 30, 2018 increased by \$1,068 to \$125,904, compared to \$124,836 for the three months ended June 30, 2017. The increase was due to additional stock options offered to employees, partially offset by stock options that have been fully expensed.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization expenses for the three months ended June 30, 2018 increased by \$137,621 to \$254,791, compared to \$117,170 for the three months ended June 30, 2017. The increase was primarily due to additional intangible assets amortized as a result of the additional fixed and intangible assets acquired from Parscale Creative and WebTegrity.

OTHER INCOME AND EXPENSE

Total other income and expense for the three months ended June 30, 2018 increased by \$44,390 to net other expense of \$93,092, compared to net other expense of \$48,702 for the three months ended June 30, 2017. The increase in net other expense was primarily due to the utilization of a secured borrowing arrangement, resulting in higher interest expense, as well as an increase in bad debt expense.

NET LOSS

The consolidated net loss for the three months ended June 30, 2018 was \$360,979, compared to the consolidated net loss of \$560,785 for the three months ended June 30, 2017. The decrease in net loss for the period was primarily due

to higher revenue, partially offset by increases in costs.

Results of Operations for the Six Months Ended June 30, 2018, compared to the Six Months Ended June 30, 2017.

REVENUE

Total revenue for the six months ended June 30, 2018 increased by \$4,264,434 to \$5,474,359, compared to \$1,209,925 for the six months ended June 30, 2017. The increase was primarily due to revenues generated from the recently acquired Parscale Creative and WebTegrity, and the addition of the newly formed Data Propria, partially offset by a reduction in revenue at Indaba.

SALARIES AND OUTSIDE SERVICES

Salaries and outside services for the six months ended June 30, 2018 increased by \$1,388,896 to \$2,952,351, compared to \$1,563,455 for the six months ended June 30, 2017. The increase was primarily due to expenses related to the recently acquired Parscale Creative and WebTegrity, and newly established Data Propria, due to additional employees added to payroll expense.

SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES

Selling, general, and administrative (“SG&A”) expenses for the six months ended June 30, 2018 increased by \$2,473,343 to \$2,933,804, compared to \$460,461 for the six months ended June 30, 2017. The increase was primarily due to

Table of Contents

operating expenses related to the recently acquired Parscale Creative and WebTegrity, and the increase in costs to maintain the additional offices in San Antonio.

STOCK BASED COMPENSATION

Stock based compensation expenses for the six months ended June 30, 2018 increased by \$37,039 to \$285,976, compared to \$248,937 for the six months ended June 30, 2017. The increase was due to additional stock options offered to employees, partially offset by stock options that have been fully expensed.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization expenses for the six months ended June 30, 2018 increased by \$328,105 to \$508,186, compared to \$180,081 for the six months ended June 30, 2017. The increase was primarily due to additional intangible assets amortized as a result of the additional fixed and intangible assets acquired from Parscale Creative and WebTegrity.

OTHER INCOME AND EXPENSE

Total other income and expense for the six months ended June 30, 2018 increased by \$103,749 to net other expense of \$182,171, compared to net other expense of \$78,422 for the six months ended June 30, 2017. The increase in net other expense was primarily due to the utilization of a secured borrowing arrangement, resulting in higher interest expense, in addition to losses incurred from the disposal of fixed assets and an increase in bad debt expense.

NET LOSS

The consolidated net loss for the six months ended June 30, 2018 was \$1,152,343, compared to the consolidated net loss of \$1,321,031 for the six months ended June 30, 2017. The decrease in net loss for the period was primarily due to higher revenue, partially offset by increases in costs.

LIQUIDITY AND CAPITAL RESOURCES

The Company had a net working capital deficit (i.e. the difference between current assets and current liabilities) of (\$3,566,559) at June 30, 2018 compared to a net working capital deficit of (\$1,835,714) at fiscal year ended December 31, 2017.

Cash flow used in operating activities was \$300,034 for the six months ended June 30, 2018, compared to cash flow used in operating activities of \$354,592 for the six months ended June 30, 2017. The decrease in cash flow used in operating activities of \$54,558 was primarily due to increases in depreciation and amortization expense and accounts payable, partially offset by increases in accounts receivable.

Cash flow used in investing activities was \$20,646 for the six months ended June 30, 2018, compared to cash flow used in investing activities of \$6,025 for the six months ended June 30, 2017. The increase in cash flow used in investing activities of \$14,621 was primarily due to the purchase of computers, partially offset by the sale of other computer equipment.

Cash flow provided by financing activities was \$792,123 for the six months ended June 30, 2018, compared to cash flow provided by financing activities of \$374,659 for the six months ended June 30, 2017. The increase in cash flow provided by financing activities of \$417,464 was due to additional borrowings, partially offset by debt repayments and

dividends paid.

Liquidity is the ability of a company to generate funds to support its current and future operations, satisfy its obligations, and otherwise operate on an ongoing basis. Significant factors in the management of liquidity are funds generated by operations, levels of accounts receivable and accounts payable and capital expenditures.

The financial statements have been prepared on a going concern basis of accounting, which contemplates continuity of operations, realization of assets and liabilities and commitments in the normal course of business. The accompanying consolidated financial statements do not reflect any adjustments that might result if we are unable to continue as a going concern. Our independent auditors, in their report on our audited financial statements for the years ended December 31, 2017 and June 30, 2017 expressed substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern is dependent upon, among other things, additional cash infusion. Management believes that the additional cash needed to meet our obligations as they become due, and which will allow the development of our core business operations, will be received through investments in the Company made by our existing shareholders, prospective new investors and future revenue generated by our operations.

As a result of the recent economic recession, and the continuing economic uncertainty, it has been difficult for companies to obtain equity or debt financing. While the credit markets have improved over the last year, it remains difficult for smaller companies to obtain financing on reasonable terms.

Any additional capital raised through the sale of equity or equity-backed securities may dilute current stockholders' ownership percentages and could also result in a decrease in the fair market value of our equity securities. The terms of the

Table of Contents

securities issued by us in future capital transactions may be more favorable to new investors and may include preferences, superior voting rights and the issuance of warrants or other derivative securities which may have a further dilutive effect.

Furthermore, any additional debt or equity or other financing that we may need may not be available on terms favorable to us, or at all. If we are unable to obtain required additional capital, we may have to curtail our growth plans or cut back on existing business. Further, we may not be able to continue operations if we do not generate sufficient revenues from operations.

We may incur substantial costs in pursuing future capital financing, including investment banking fees, legal fees, accounting fees, securities law compliance fees, printing and distribution expenses and other costs. We may also be required to recognize non-cash expenses in connection with certain securities we issue, such as convertible notes and warrants, which may adversely impact our reported financial results.

Off-Balance Sheet Arrangements

None.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Management, with the participation of the Company's principal executive and principal financial officers, or persons performing similar functions, evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act of 1934, as amended), as of the end of the period covered by this report to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Act is (i) recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Based on that evaluation, our management concluded that, as of June 30, 2018, our disclosure controls and procedures were not effective due to the following material weaknesses:

1. lack of segregation of duties; and
2. failure to implement accounting controls of acquired businesses.

To the extent reasonably possible given our limited resources, we intend to take measures to cure the aforementioned weaknesses.

Our management, including our principal executive officer and principal financial officer, do not expect that our disclosure controls and procedures or our internal controls will prevent all error or fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints

and the benefits of controls must be considered relative to their costs. Due to the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

To address the material weaknesses, we performed additional analysis and other post-closing procedures in an effort to ensure our consolidated financial statements included in this report have been prepared in accordance with generally accepted accounting principles. Accordingly, management believes that the financial statements included in this report fairly present in all material respects our financial condition, results of operations and cash flows for the periods presented.

No Attestation Report by Independent Registered Accountant

The effectiveness of our internal control over financial reporting as of June 30, 2018 has not been audited by our independent registered public accounting firm by virtue of our exemption from such requirement as a smaller reporting company.

Table of Contents

Changes in Internal Controls over Financial Reporting

There have been no changes in the Company's internal control over financial reporting that occurred during the Company's last fiscal quarter ended June 30, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

The Company's management does not expect that its disclosure controls or its internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

PART II. - OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

The Company may be involved in legal actions and claims arising in the ordinary course of business from time to time in the future. However, at this time there are no current legal proceedings to which the Company or any of its subsidiaries is a party or of which any of their property is the subject.

Item 1A. RISK FACTORS

There have been no material changes to the risk factors disclosed in "Risk Factors" in our transition report on Form 10-KT/A filed with the SEC on June 18, 2018.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Item 5. OTHER INFORMATION

None

Item 6. EXHIBITS

(a) Exhibits

| EXHIBIT NO. | DESCRIPTION |
|-------------|--|
| 31.1 | <u>Section 302 Certification</u> |
| 31.2 | <u>Section 302 Certification</u> |
| 32.1 | <u>Section 906 Certification</u> |
| 32.2 | <u>Section 906 Certification</u> |
| EX-101.INS | XBRL INSTANCE DOCUMENT* |
| EX-101.SCH | XBRL TAXONOMY EXTENSION SCHEMA DOCUMENT* |
| EX-101.CAL | XBRL TAXONOMY EXTENSION CALCULATION LINKBASE* |
| EX-101.DEF | XBRL TAXONOMY EXTENSION DEFINITION LINKBASE* |
| EX-101.LAB | XBRL TAXONOMY EXTENSION LABELS LINKBASE* |
| EX-101.PRE | XBRL TAXONOMY EXTENSION PRESENTATION LINKBASE* |

* Furnished herewith. Pursuant to Rule 406T of Regulation S-T, the interactive data files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, and otherwise are not subject to liability under those sections.

32

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CLOUDCOMMERCE, INC.
(Registrant)

Dated: August 14, 2018 By: */s/ Andrew Van Noy*
Andrew Van Noy

Chief Executive Officer and President

(Principal Executive Officer)

/s/ Gregory Boden
Gregory Boden

Chief Financial Officer

(Principal Financial and Accounting Officer)