



# Quadlogic Controls Corporation

Financial Statements  
Years Ended February 28, 2018 and 2017

# Quadlogic Controls Corporation

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Financial Statements  
Years Ended February 28, 2018 and 2017

# Quadlogic Controls Corporation

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Tel: 631-501-9600  
Fax: 631-501-1885  
www.bdo.com

401 Broadhollow Road, Suite 201  
Melville, NY 11747

## Independent Auditor's Report

The Board of Directors  
Quadlogic Controls Corporation  
Long Island City, New York

We have audited the accompanying financial statements of Quadlogic Controls Corporation, which comprise the balance sheets as of February 28, 2018 and 2017, and the related statements of income, changes in shareholders' deficit and cash flows for the years then ended, and the related notes to the financial statements.

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

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

### *Auditor's Responsibility*

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

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

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

*Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Quadlogic Controls Corporation as of February 28, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

BDO USA, LLP

August 3, 2018

# Quadlogic Controls Corporation

## Balance Sheets

<i>February 28,</i>	2018	2017
<b>Assets</b>		
<b>Current Assets</b>		
Cash	\$ 128,094	\$ 128,083
Accounts receivable, trade, net of allowance for doubtful accounts of \$73,437 and \$94,937 in 2018 and 2017	1,754,430	2,018,112
Inventories	1,361,031	1,562,544
Prepaid expenses and other current assets	170,311	195,245
<b>Total Current Assets</b>	<b>3,413,866</b>	<b>3,903,984</b>
<b>Property and Equipment, Net</b>	<b>648,650</b>	<b>842,379</b>
<b>Other Assets</b>		
Other assets	388,915	354,437
Patent and trademark costs, net of accumulated amortization of \$142,964 in 2018 and \$115,993 in 2017	385,616	434,298
Lease deposits	191,854	191,854
<b>Total Other Assets</b>	<b>966,385</b>	<b>980,589</b>
<b>Total Assets</b>	<b>\$ 5,028,901</b>	<b>\$ 5,726,952</b>
<b>Liabilities and Shareholders' Deficit</b>		
<b>Current Liabilities</b>		
Current maturities of installment debt	\$ -	\$ 28,431
Accounts payable	1,418,533	1,825,685
Customer deposits	102,809	189,933
Current portion of accrued compensation	677,703	689,084
Accrued expenses and other liabilities	779,673	829,648
<b>Total Current Liabilities</b>	<b>2,978,718</b>	<b>3,562,781</b>
<b>Non-Current Liabilities</b>		
Accrued compensation	376,852	462,023
Secured line of credit - borrowings	938,275	610,922
Other non-current liabilities	801,836	1,165,171
<b>Total Non-Current Liabilities</b>	<b>2,116,963</b>	<b>2,238,116</b>
<b>Total Liabilities</b>	<b>5,095,681</b>	<b>5,800,897</b>
<b>Commitments</b>		
<b>Shareholders' Deficit</b>		
Common stock - \$0.001 par value; 20,000,000 shares authorized, 11,373,351 and 11,373,351 shares issued and outstanding in 2018 and 2017, respectively	11,373	11,373
Additional paid-in capital	9,499,549	9,499,549
Accumulated deficit	(9,577,702)	(9,584,867)
<b>Total Shareholders' Deficit</b>	<b>(66,780)</b>	<b>(73,945)</b>
<b>Total Liabilities and Shareholders' Deficit</b>	<b>\$ 5,028,901</b>	<b>\$ 5,726,952</b>

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Statements of Income

<i>Year ended February 28,</i>	2018	2017
<b>Revenues</b>		
Meter sales	\$ 7,259,784	\$ 7,097,931
Royalty income	1,000,000	1,150,000
Billing and technical services	5,542,408	5,158,872
<b>Total Revenues</b>	<b>13,802,192</b>	<b>13,406,803</b>
<b>Cost of Goods Sold</b>		
Cost of meters sold	4,854,540	4,670,686
Cost of billing and technical services	2,969,308	2,894,089
<b>Total Cost of Goods Sold</b>	<b>7,823,848</b>	<b>7,564,775</b>
Gross Profit	5,978,344	5,842,028
<b>Operating Expenses</b>		
Selling	1,598,198	1,525,741
Research and development	1,319,852	1,519,604
General and administrative	2,878,891	2,308,193
<b>Total Operating Expenses</b>	<b>5,796,941</b>	<b>5,353,538</b>
Operating Income	181,403	488,490
<b>Other Expense</b>		
Interest expense	(143,249)	(171,584)
Other expense, net	(30,989)	(30,137)
<b>Total Other Expense</b>	<b>(174,238)</b>	<b>(201,721)</b>
<b>Net Income</b>	<b>\$ 7,165</b>	<b>\$ 286,769</b>

*See accompanying notes to financial statements.*

**Quadlogic Controls Corporation**  
**Statements of Changes in Shareholders' Deficit**

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*Years ended February 28, 2018 and 2017*

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total
	Number of Shares	Par Value			
<b>Balance, February 29, 2016</b>	11,313,351	\$ 11,313	\$ 9,484,609	\$ (9,871,636)	\$ (375,714)
Stock granted to directors	60,000	60	14,940	-	15,000
Net income	-	-	-	286,769	286,769
<b>Balance, February 28, 2017</b>	11,373,351	11,373	9,499,549	(9,584,867)	(73,945)
Net income	-	-	-	7,165	7,165
<b>Balance, February 28, 2018</b>	11,373,351	\$ 11,373	\$ 9,499,549	\$ (9,577,702)	\$ (66,780)

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Statements of Cash Flows

<i>Year ended February 28,</i>	2018	2017
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 7,165	\$ 286,769
Adjustment to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	212,700	207,079
Provision for doubtful accounts	3,780	1,388
Stock-based compensation	-	15,000
Write-off patents	36,957	10,449
Loss on abandoned equipment	35,300	-
Changes in assets and liabilities:		
Accounts receivable	259,902	175,581
Inventories	167,035	(38,422)
Prepaid expenses and other current assets	24,934	240,334
Accounts payable	(407,152)	153,703
Customer deposits	(87,124)	61,995
Accrued expenses and other liabilities	(231,593)	238,660
Accrued compensation	(96,552)	(7,490)
Other non-current liabilities	(181,717)	(64,049)
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>(256,365)</b>	<b>1,280,997</b>
<b>Cash Flows from Investing Activities</b>		
Purchase of property and equipment	(27,300)	(158,745)
Patent acquisition costs	(15,246)	(9,782)
<b>Net Cash Provided by (Used in) Investing Activities</b>	<b>(42,546)</b>	<b>(168,527)</b>
<b>Cash Flows from Financing Activities</b>		
Principal payments on debt	(28,431)	(277,635)
Borrowing from line of credit	14,335,000	13,458,912
Repayments of line of credit	(14,007,647)	(14,436,368)
<b>Net Cash Provided by (Used in) Financing Activities</b>	<b>298,922</b>	<b>(1,255,091)</b>
<b>Net Increase (Decrease) in Cash</b>	<b>11</b>	<b>(142,621)</b>
Cash, beginning of year	128,083	270,704
<b>Cash, end of year</b>	<b>\$ 128,094</b>	<b>\$ 128,083</b>
<b>Supplemental Disclosure of Cash Flow Information</b>		
Interest paid	\$ 112,793	\$ 305,929

### Supplemental Disclosures of Noncash Investing and Financing Activities

During the year ended February 28, 2017, prepaid insurance amounting to \$28,431 was financed by installment notes in 2017.

*See accompanying notes to financial statements.*

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 1. Summary of Significant Accounting Policies

This summary of the significant accounting policies of Quadlogic Controls Corporation (Quadlogic, or the Company) is presented to assist in the understanding of the financial statements. The financial statements and notes are representations of the Company's management, which is responsible for the integrity and objectivity of the financial statements. These accounting policies conform to U.S. generally accepted accounting principles, and have been consistently applied in the preparation of the financial statements.

#### *History and Business Activity*

The Company is engaged in the business of electricity metering, monitoring and control. All Quadlogic metering products feature the Company's proprietary robust power line communications technology. The business consists of four segments. First is the design, manufacture and sale of the "smart" metering systems, a line of digital, microprocessor controlled meters that, in communication with the Quadlogic Transponder, measure and remotely monitor the time and amount of electricity consumption, and perform other diagnostics. The second segment supports the first and consists of technical services including meter reading, customer billing, and system repair and maintenance. The third segment, the Energy Guard™ system of concentrated metering, is sold primarily to utilities in countries where electricity theft is common. It consists of pole-mounted sealed panels of meters, remote data concentrators, and sub-station based data collectors capable of remote metering, theft and tamper detection and remote power disconnect and reconnect. The fourth segment is comprised of royalties from licensees producing and selling the Company's Energy Guard systems under licensing agreements. The Company's revenues for the fiscal years ended February 28, 2018 and 2017 were generated from sales to foreign customers of 29.4% and 30.9%, respectively. Canadian sales represented approximately 29.2% and 30.3% and other foreign sales represented 0.2% and 0.5% of total revenues for the fiscal years ended February 28, 2018 and 2017, respectively. In addition, the Company has recorded royalty income from Mexico of \$1,000,000 and \$1,150,000 as of February 28, 2018 and 2017, respectively. The Company's customers include real estate development and construction companies, owners and operators of multi-tenant commercial and residential buildings, distributors, foreign electric utility companies and licensees.

The Company's stock is not listed on any organized exchange but is traded on the over-the-counter market. The Company's common stock is quoted on the OTC Markets (Pink) and experiences limited trading activity.

#### *Use of Estimates*

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### *Accounts Receivable*

The Company carries its accounts receivable at cost less allowances for doubtful accounts and returns. On a periodic basis, the Company evaluates its accounts receivable and establishes

# Quadlogic Controls Corporation

## Notes to Financial Statements

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allowances for doubtful accounts and returns based on a history of past write-offs, collections, returns and current conditions.

### *Revenue Recognition*

The Company recognizes revenue from the sale of electric metering equipment at the time of shipment to the customer. Revenues from meter read and bill services, and from repair and technical services are recognized at the time the services are rendered. The Company has entered into certain arrangements with a customer to license technology. The customer is obligated to pay royalties to the Company when the product is shipped to the end user.

### *Fair Value of Financial Instruments*

The Company follows the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, "Fair Value Measurement," which defines fair value 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 820 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs).

The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under ASC 820 are described as follows:

*Level 1* - These are unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date.

*Level 2* - These are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

*Level 3* - These are inputs that are unobservable for the asset or liability.

The carrying value of the Company's cash, accounts receivable and accounts payable approximates their fair values based on the short-term nature of such items. The carrying value of the installment debt and secured line of credit approximates fair value since the interest rate is at terms currently available to the Company.

### *Inventories*

Inventories are stated at the lower of cost or market, with cost determined on the first-in, first-out basis.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### *Depreciation and Amortization*

Depreciation and amortization are provided principally on the straight-line method over the estimated useful lives of the related assets, as follows:

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Machinery and equipment	5 years
Office furniture and equipment	3-7 years
Computer equipment and software costs	3-5 years
Tools, dies and molds	3 years

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Leasehold improvements are amortized over the lesser of the estimated useful life of the asset or the term of the lease.

Expenditures for maintenance and repairs are expensed as incurred, while renewals and betterments that materially extend the life of an asset are capitalized. The cost of assets sold, retired, or otherwise disposed of, and the related allowance for depreciation, are eliminated from the accounts, and any resulting gain or loss is recognized.

### *Patents*

The Company owns various patents of technology concerning its electronic metering systems and processes. The costs associated with the acquisition of patents, and the costs of registering the patents, are capitalized and amortized on the straight-line basis over their remaining lives. Amortization expense for the fiscal years ended February 28, 2018 and 2017 amounted to approximately \$25,000 and \$24,000, respectively.

### *Trademarks*

The Company owns two trademarks in various countries. The cost of registering the trademarks are capitalized and amortized on the straight-line basis over the remaining lives. Amortization expense for the fiscal years ended February 28, 2018 and 2017 amounted to approximately \$2,300 for each year.

### *Research and Development*

Research and development costs are expensed as incurred.

### *Shipping and Handling*

Shipping and handling costs incurred in shipping products to customers are expensed as incurred and included in cost of meters sold. Shipping costs totaled approximately \$122,000 and \$87,000 for the fiscal years ended February 28, 2018 and 2017, respectively. All shipping and handling costs billed to customers are recorded in revenue.

### *Stock-based Compensation*

The Company follows the provisions of ASC 718 for stock-based compensation. This statement requires entities to measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award over the service period.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 2. Deferred Taxes

The Company provides for income taxes and recognizes deferred tax assets and liabilities on the balance sheet using the liability method for income taxes. The liability method requires that all deferred tax balances be determined by using the applicable tax rate expected to be in effect when the taxes will actually be paid, or when refunds are received. The applicable tax rate is applied to the differences between the tax bases of assets and liabilities and to their reported amounts in the financial statements. The resulting deferred tax asset or liability is adjusted to reflect changes in tax laws as they occur. Valuation allowances are established, if necessary, to reduce the deferred tax assets and liabilities (see Note 11).

### 3. Concentration of Credit Risk

The Company maintains its cash balances in financial institutions in New York. From time to time, the Company has cash balances that may exceed federally insured limits.

The Company's trade receivables are potentially subject to credit risk. The Company extends credit to its customers based upon an evaluation of the customers' financial condition and credit history. The Company's policies do not require collateral to support accounts receivable. However, because of the diversity and creditworthiness of the individual accounts that comprise the total balance, management does not believe that the Company is subject to any significant credit risk.

For the fiscal years ended February 28, 2018 and 2017, revenues derived from two customers amounted to \$2,328,843 or 16.9% and \$2,610,496 or 21.3% of total revenues, respectively. For the same periods, accounts receivable from three customers accounted for 32.6% and 33.3% of total receivables, and accounts receivable for one customer accounted for the fiscal years ended February 28, 2018 and 2017 was 18.4% and 22.2%, respectively.

### 4. Inventories

Inventories consisted of the following:

<i>February 28,</i>		2018		2017
Raw materials	\$	453,599	\$	435,541
Work-in-progress		504,959		698,164
Finished goods		402,473		428,839
<b>Total Inventories</b>	<b>\$</b>	<b>1,361,031</b>	<b>\$</b>	<b>1,562,544</b>

# Quadlogic Controls Corporation

## Notes to Financial Statements

### 5. Property and Equipment

Property and equipment consisted of the following:

<i>February 28,</i>	2018	2017
Machinery and equipment	\$ 1,229,919	\$ 1,248,005
Office furniture and equipment	416,141	416,140
Leasehold improvements	1,574,146	1,574,147
Computer equipment and software costs	181,177	181,177
Tools, dies and molds	242,860	263,110
	<b>3,644,243</b>	<b>3,682,579</b>
Less: Accumulated depreciation and amortization	<b>(2,995,593)</b>	<b>(2,840,200)</b>
<b>Property and Equipment, net</b>	<b>\$ 648,650</b>	<b>\$ 842,379</b>

Depreciation and amortization expense for the fiscal years ended February 28, 2018 and 2017 amounted to approximately \$186,000 and \$181,000, respectively.

### 6. Intangible Assets

The components and weighted average amortization period of intangible assets are as follows:

<i>February 28,</i>	2018	2017	Weighted Average Amortization Period
Patents	\$ 498,617	\$ 515,106	18 years
Trademarks	29,964	35,185	10 years
Gross intangibles	528,581	550,291	
Less: Accumulated amortization (patents)	(128,559)	(103,936)	
Less: Accumulated amortization (trademarks)	(14,406)	(12,057)	
<b>Intangibles, net of amortization</b>	<b>\$ 385,616</b>	<b>\$ 434,298</b>	

The aggregate amortization expense related to intangible assets for the next five years is as follows:

<i>Year ending February 28,</i>	
2019	\$ 30,697
2020	30,697
2021	30,697
2022	30,697
2023	30,697
2024 and thereafter	232,131
<b>Total</b>	<b>\$ 385,616</b>

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 7. Secured Credit Line

On October 1, 2012, the Company entered into a new two-year loan agreement expiring October 1, 2014. On January 22, 2018, the loan agreement was amended to continue in full force and affect for a term ending October 31, 2019, and shall automatically renew from year to year thereafter until terminated by either party for a \$2,000,000 total revolving line of credit facility with Entrepreneur Growth Capital, LLC (EGC). The maximum loans and advances against accounts receivable is \$2,000,000 and against inventory is \$250,000. EGC agrees, at borrower's request, to periodically re-evaluate the total facility, and may increase the facility, but not to exceed \$5,000,000. This line of credit is secured by the Company's trade receivables, deposit accounts, equipment, machinery, and furniture and fixtures. Borrowings under the credit facility bear interest at prime plus 3% for loans made against accounts receivable, and interest at prime plus 5% for loans made against inventory. The minimum monthly interest charge is \$4,000 for a credit line of \$1,250,000 and increases to \$5,000 when the total credit line exceeds \$1,250,000. The agreement includes collateral monitoring fees and an annual facility fee of 2% on the line of credit. The amount borrowed at February 28, 2018 and 2017 was approximately \$938,000 and \$611,000, respectively.

### 8. Installment Debt

Installment debt consists of the following:

<i>February 28,</i>	2018	2017
Unsecured loan payables to Bank Direct Capital Finance, which bear interest at 5.95% and 6.2% per annum for directors and officers, and errors and omissions insurance effective December 27, 2015 and December 18, 2015, respectively. The loans finance corporate insurance premiums. The loans required down payments of \$11,000 and \$11,846 with principal balance due of \$33,000 and \$34,103, and nine monthly payments of \$3,758.17 and \$3,887.73. For fiscal year ended February 28, 2018, interest was 5.45%. Total down payment was \$22,890, with principal balance due of \$68,671 and nine monthly payments of \$7,804.40.	\$ -	\$ 28,431
Total	-	28,431
Less: Current Portion	-	28,431
Long-Term Portion	\$ -	\$ -

### 9. Convertible Preferred Stock

The Company is authorized to issue 5,000,000 shares of \$.001 par value preferred stock, including 4,000,000 shares of Series A convertible preferred stock. The shares may be designated and issued by the Board of Directors at any time in one or more series that will have voting rights, mandatory interest, convertible features, and/or preferences that have not been given to shares of any other series of the Company's common stock. No shares were issued or outstanding as of February 28, 2018 and 2017.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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Series A convertible preferred stock accrues cumulative dividends at the rate of 9% per annum, which are payable if and when declared by the Company's Board. Each share of preferred stock is convertible into 1.25 shares of common stock at the option of the holder at any time.

### 10. Commitments

In fiscal year 2007, the Company entered into a lease agreement for new facilities. The lease commenced July 1, 2007, and expires December 31, 2022. The lease is for a 15-year period, with an option to buy out the remainder of the lease term at the end of 10 years. The lease provides for minimum annual rentals plus real estate taxes and escalation charges. The new facilities are located within an area that qualifies the Company for certain New York City income tax credits.

Rent expense charged to operations, net of income tax credits, amounted to approximately \$991,000 and \$854,000 for the fiscal years ended February 28, 2018 and 2017, respectively.

Future minimum annual rental payments under the non-cancelable operating lease are as follows:

*Year ending February 28,*

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2019		\$	943,916
2020			943,916
2021			943,916
2022			943,916
2023			314,639
		\$	4,090,303

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### *Concentration of Vendors*

The Company relies on a limited number of outside vendors who currently supply necessary components for the manufacture of meters. The Company is subject to the risk that it may not be able to obtain sufficient quantities or reasonable prices. The Company purchased inventory and services from its three largest vendors of \$1,180,195 and \$909,523 for the years ended February 28, 2018 and 2017, respectively. This represents 23.2% and 17.9% of the total purchases for years ended February 28, 2018 and 2017, respectively.

### 11. Income Taxes

Deferred tax assets arise from net operating loss carryforwards and from items that are currently expensed for financial statement purposes but are not currently deductible for income tax purposes. The components of the deferred tax asset are as follows:

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<i>February 28,</i>		2018		2017
<b>Current Deferred Tax Assets</b>				
Accrued expenses	\$	214,145	\$	245,018
Deferred rent		172,049		346,855
Other reserves		140,587		126,480
Tax capitalization of certain inventory costs		38,573		184,719
Royalty income		180,850		1,700,000
<b>Total Current Deferred Tax Assets</b>	\$	746,204	\$	2,603,072

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# Quadlogic Controls Corporation

## Notes to Financial Statements

<i>February 28,</i>	2018	2017
<b>Long-Term Deferred Tax Assets</b>		
Net operating loss carryforwards	\$ 516,794	\$ 389,207
R&D credit carryforwards	1,019,735	922,552
REAP credit carryforward	1,098,638	905,288
Wage reduction credit	9,600	-
<b>Total Long-Term Deferred Tax Assets</b>	<b>2,644,767</b>	<b>2,217,047</b>
<b>Long-Term Deferred Tax Liability</b>		
Depreciation	(20,127)	(37,426)
<b>Net Long-Term Deferred Tax Assets</b>	<b>2,624,640</b>	<b>2,179,621</b>
<b>Total Deferred Tax Assets</b>	<b>3,370,844</b>	<b>4,782,693</b>
<b>Less: Valuation Allowance</b>	<b>(3,370,844)</b>	<b>(4,782,693)</b>
<b>Net Deferred Tax Asset</b>	<b>\$ -</b>	<b>\$ -</b>

The Company has established a full valuation allowance against its deferred tax assets due to the uncertainty surrounding realization of such assets.

At February 28, 2017 the Company measured its deferred tax items at an effective federal tax rate of 34%. On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the Act) was signed into law. Among other things, the Act reduced the Company's corporate federal tax rate to a flat 21%. As a result, the Company's deferred tax items are measured at an effective tax rate of 21% for federal tax purposes as of February 28, 2018.

As of February 28, 2018, the Company had federal, state and city net operating loss carryforwards of approximately \$3,370,844, available to reduce any future federal taxable income. The federal net operating loss carryforwards begin expiring in February 28, 2030.

The Company follows ASC 740-10 (FASB Interpretation No. 48) "Accounting for Uncertainty in Income Taxes," which clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statement disclosure of tax provisions taken or expected to be taken on a tax return. The Company has not identified any uncertain tax positions that would require a provision of a liability under ASC 740-10.

Open tax years for Federal income taxes are fiscal years ended 2018, 2017, 2016 and 2015. Open tax years for state income taxes range between three to four years or for fiscal years ended 2014 to 2018.

The Company's policy is to recognize interest and penalties relating to uncertain tax positions in income tax expense.

## 12. Employee Benefit Plan

The Company maintains a 401(k) plan. The plan covers all full-time employees with a minimum of three months of service. The plan includes a discretionary match at the Company's option. However no match was funded by the Company for the fiscal years ended February 28, 2018 and 2017.

# Quadlogic Controls Corporation

## Notes to Financial Statements

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### 13. Employee Stock Option Plan and Warrants

The Company recognized no compensation expense arising from stock options issued to employees for fiscal years ended 2018 and 2017, respectively.

On September 1, 1999, the Board of Directors adopted the 1999 Stock Option Plan (the 1999 Plan). This was approved by the shareholders in April 2000. The 1999 Plan provides for the granting of options to officers, directors, employees, and consultants to purchase up to 2,000,000 shares of the Company's common stock. The 1999 Plan expired September 2009.

There were no outstanding options for the fiscal years ended February 28, 2018 and 2017. A summary of stock option activity related to the Company's 1999 Stock Option Plan for the fiscal year ended February 28, 2017 is as follows:

	Number of Shares	Weighted Average Exercise Price Per Share	Expiration Date of Options
Outstanding, February 29, 2016	20,000	1.25	May 18, 2016
Forfeited	(20,000)		
Outstanding, February 28, 2017	-	\$ -	

The Company compensates each independent director \$40,000 annually and grants each independent director up to 30,000 shares of the Company's common stock which vest immediately. There was no stock granted to directors in fiscal year 2018 and 60,000 shares granted in fiscal year 2017.

As of February 28, 2018 and 2017, there were no outstanding directors' options.

#### *Warrants*

The Company has granted warrants to purchase shares of its common stock in connection with various equity transactions. There were 249,760 warrants outstanding during the years ended February 28, 2018 and 2017.

There were no warrants issued for fiscal years ended February 28, 2018 and 2017.

The Company uses the Black-Scholes pricing model to value warrants. The value of each warrant granted is estimated on the date of the grant.

### 14. Related Party Transactions

Accrued compensation includes accrued unpaid compensation payable to one of the Company's officers (who is also a significant shareholder). The obligation is unsecured and bears interest at 6% per annum. Interest accrued on unpaid compensation for the fiscal years ended February 28, 2018 and 2017 was \$33,350 and \$37,072, respectively. The current portion of accrued compensation at February 28, 2018 and 2017 includes \$118,467 and \$148,533, respectively, of the unpaid officer's compensation payable. The balance due to an officer of \$376,852 and \$462,023, at February 28, 2018

# Quadlogic Controls Corporation

## Notes to Financial Statements

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and 2017, is classified as non-current, as the officer has agreed to not call the unpaid balance before March 1, 2019.

### **15. Litigation**

From time to time, the Company is involved in routine litigation that arises in the ordinary course of business. There are no pending significant legal proceedings to which the Company is a party for which management believes the ultimate outcome would have a material adverse effect on the Company's financial position. On January 16, 2018, the Company filed lawsuits against its Mexican licensee and its former employee alleging among other things, breach of contract, failure to pay royalties, and breach of fiduciary duty and seeking injunctive relief, payment of royalties in the amount of \$7,360,000, and full access to Energy Guard source code. The lawsuits are in the early stages and no assurances of recovery or the amount can be made.

### **16. Subsequent Events**

Subsequent events have been evaluated through August 3, 2018, which is the date the financial statements were available to be issued.