MobileSmith, Inc.
Form 10-Q
August 04, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 001-32634

MOBILESMITH, INC.
(Exact name of registrant as specified in its charter)

Delaware	95-4439334
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

5400 Trinity Road, Suite 208 Raleigh, North Carolina	27607
(Address of principal executive offices)	(Zip Code)

(855) 516-2413
(Registrant's telephone number, including area code)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

As of August 3, 2016, there were 19,827,542 shares of the registrant’s common stock, par value $0.001 per share, outstanding.

MOBILESMITH, INC.

FORM 10-Q
For the Quarterly Period Ended June 30, 2016

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PART I – FINANCIAL INFORMATION
MOBILESMITH, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

	June 30, 2016	December 31, 2015
Current Assets		
Cash and Cash Equivalents	$582,027	$580,220
Restricted Cash	125,001	124,988
Trade Accounts Receivable, Net of Allowance for Doubtful Accounts of $99,300 and $16,050, Respectively	399,257	183,350
Prepaid Expenses and Other Current Assets	70,387	69,552
Total Current Assets	1,176,672	958,110
Property & Equipment, Net	96,764	98,963
Capitalized Software, Net	336,505	390,518
Intangible Assets, Net	46,352	55,099
Other Assets	-	6,264
Total Other Assets	479,621	550,844
Total Assets	$1,656,293	$1,508,954
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current Liabilities		
Trade Accounts Payable	$86,658	$45,717
Accrued Expenses	225,486	247,858
Accrued Interest	369,895	350,613
Capital Lease Obligations	32,208	30,877
Deferred Revenue	1,560,718	1,007,970
Bank Loan	-	5,000,000
Convertible Notes Payable, Related Parties, Net of Discount	-	33,363,488
Convertible Notes Payable, Net of Discount	-	680,640
Total Current Liabilities	2,274,965	40,727,163
Long-Term Liabilities		
Bank Loan	5,000,000	-
Convertible Notes Payable, Related Parties, Net of Discount	36,531,560	-
Convertible Notes Payable, Net of Discount	680,640	-
Capital Lease Obligations	67,317	83,761
Deferred Rent	48,264	53,592

Total Long-Term Liabilities	42,327,781	137,353
Total Liabilities	44,602,746	40,864,516
Commitments and Contingencies (Note 3)		
Stockholders' Deficit		
Preferred Stock, $0.001 Par Value, 5,000,000 Shares Authorized, No Shares Issued and Outstanding at June 30, 2016 and December 31, 2015	-	-
Common Stock, $0.001 Par Value, 100,000,000 and 45,000,000 Shares Authorized At June 30, 2016 and December 31, 2015, Respectively; 19,827,542 Shares Issued and Outstanding at June 30, 2016 and December 31, 2015	19,828	19,828
Additional Paid-in Capital	98,062,577	97,545,601
Accumulated Deficit	(141,028,858)	(136,920,991)
Total Stockholders' Deficit	(42,946,453)	(39,355,562)
Total Liabilities and Stockholders' Deficit	$1,656,293	$1,508,954

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

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MOBILESMITH, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2016	June, 30 2015	June, 30 2016	June, 30 2015
REVENUES:				
Subscription and Support	$494,169	$377,545	$965,299	$773,733
Professional Services and Other	4,154	30,000	4,154	60,000
Total Revenue	498,323	407,545	969,453	833,733
COST OF REVENUES:				
Subscription and Support	93,048	74,229	208,369	133,698
Professional Services and Other	51,179	14,272	56,242	23,545
Total Cost of Revenue	144,227	88,501	264,611	157,243
GROSS PROFIT	354,096	319,044	704,842	676,490
OPERATING EXPENSES:				
Sales and Marketing	325,450	267,047	561,174	559,246
Research and Development	400,856	333,685	807,399	673,825
General and Administrative	399,388	283,887	752,361	598,453
Total Operating Expenses	1,125,694	884,619	2,120,934	1,831,524
LOSS FROM OPERATIONS	(771,598)	(565,575)	(1,416,092)	(1,155,034)
OTHER INCOME (EXPENSE):				
Other Income	3,529	1,111	11,568	1,490
Interest Expense, Net	(1,221,447)	(1,311,617)	(2,703,343)	(2,578,753)
Total Other Expense	(1,217,918)	(1,310,506)	(2,691,775)	(2,577,263)
NET LOSS	$(1,989,516)	$(1,876,081)	$(4,107,867)	$(3,732,297)
NET LOSS PER COMMON SHARE:				
Basic and Fully Diluted	$(0.10)	$(0.09)	$(0.21)	$(0.19)
WEIGHTED-AVERAGE NUMBER OF SHARES USED IN COMPUTING NET LOSS PER COMMON SHARE:				
Basic And Fully Diluted	19,827,542	19,827,542	19,827,542	19,827,542

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

MOBILESMITH, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Six Months Ended	
	June 30,	June 30,
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Loss	$(4,107,867)	$(3,732,297)
Adjustments to Reconcile Net Loss to Net Cash Used in Operating Activities:		
Depreciation and Amortization	81,624	81,007
Bad Debt Expense (Gain on Reversal of Bad Debt)	83,250	(6,000)
Amortization of Debt Discount	1,092,547	1,166,864
Share Based Compensation	42,501	42,617
Changes in Assets and Liabilities:		
Accounts Receivable	(299,157)	(93,822)
Prepaid Expenses and Other Assets	5,429	(4,069)
Accounts Payable	40,941	(51,949)
Deferred Revenue	552,748	50,507
Accrued and Other Expenses	(8,418)	(149,735)
Net Cash Used in Operating Activities	(2,516,402)	(2,696,877)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments to Acquire Property, Plant and Equipment	(16,665)	(9,683)
Net Cash Used in Investing Activities	(16,665)	(9,683)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Restricted Cash Used to Pay Interest Expense	114,112	97,385
Deposit of Cash to Restricted Account	(114,125)	(97,385)
Proceeds From Issuance of Long Term Debt	2,550,000	3,200,000
Repayments of Debt Borrowings	(15,113)	(13,556)
Net Cash Provided by Financing Activities	2,534,874	3,186,444
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,807	479,884
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	580,220	320,286
CASH AND CASH EQUIVALENTS, END OF PERIOD	$582,027	$800,170
Supplemental Disclosures of Cash Flow Information:		
Cash Paid During the Period for Interest	$1,570,647	$1,558,498

Non-Cash Investing and Financing Activities		
The Company Recorded Debt Discount Associated with Beneficial Conversion Feature	$474,475	$-

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

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MOBILESMITH, INC.
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT
FOR THE PERIOD ENDED JUNE 30, 2016
(unaudited)

	Common Stock		Additional		
	Shares	$0.001 Par Value	Paid-In Capital	Accumulated Deficit	Totals
BALANCES, DECEMBER 31, 2015	19,827,542	$19,828	$97,545,601	$(136,920,991)	$(39,355,562)
Equity-Based Compensation		-	42,501	-	42,501
Beneficial Conversion Feature Recorded as a Result of Issuance of Convertible Debt		-	474,475	-	474,475
Net Loss		-	-	(4,107,867)	(4,107,867)
BALANCES, JUNE 30, 2016	19,827,542	$19,828	$98,062,577	$(141,028,858)	$(42,946,453)

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

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MOBILESMITH, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the Quarterly Period Ended June 30, 2016
(unaudited)

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

MobileSmith, Inc. (referred to herein as the "Company," "us," "we," or "our") was incorporated as Smart Online, Inc. in the State of Delaware in 1993. The Company changed its name to MobileSmith, Inc. effective July 1, 2013. The Company develops software products and services and targets businesses who need to connect with their stakeholders (customers, employees, broader public) through a variety of mobile devices and do so within the fastest time to market possible, while by-passing the need to write a single line of code. The Company's flagship product is the MobileSmith® Platform (the "Platform"). The Platform is an innovative app development platform that enables organizations to rapidly create, deploy, and manage custom, native smartphone and tablet apps deliverable across iOS and Android mobile platforms without writing a single line of code.

These condensed consolidated financial statements include accounts of the Company and its wholly-owned subsidiary, which was created to explore the concept of a consumer targeted mobile app development platform. From time to time, the Company may create additional wholly-owned subsidiaries in order to test various new services as a part of its research and development process. The subsidiary has not had material activity in 2016.

The Company's principal products and services include:

subscription to its Software as a Service ("SaaS") cloud based mobile app development platform to customers who design and build their own apps;

dedicated internal and secure mobile development platform for the U.S. Department of Defense and related contractors;

custom mobile application design and development services;

mobile application marketing services; and

mobile strategy implementation consulting.

The Company prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its audited annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). In management's opinion, the Company has made all adjustments (consisting only of normal, recurring adjustments, except as otherwise indicated) necessary to fairly present its financial position, results of operations, cash flows, and stockholders' deficit as of June 30, 2016. The Company's interim period operating results do not necessarily indicate the results that may be expected for any other interim period or for the full fiscal year. These condensed consolidated financial statements and accompanying notes should be read in conjunction with the audited annual consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015 on file with the SEC (the "Annual Report")

Except as otherwise noted, there have been no material changes to the Company's significant accounting policies as compared to the significant accounting policies described in the Annual Report. The accompanying condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. During the six months ended June 30, 2016 and 2015, the Company incurred net losses as well as negative cash flows from operations. These factors raise substantial doubt about the Company's ability to continue as a going concern. The accompanying condensed consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts or classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

Recently Issued Accounting Pronouncements

The Company evaluates new significant accounting pronouncements at each reporting period. For the period ended June 30, 2016, the Company did not adopt any new pronouncement that had or is expected to have a material effect on the Company's presentation of its condensed consolidated financial statements.
In March 2016, the FASB, issued a new accounting standard intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. The new guidance includes provisions to reduce the complexity related to income taxes, statement of cash flows, and forfeitures when accounting for share-based payment transactions. The new standard is effective for annual periods beginning after December 15, 2016, and interim periods within annual periods beginning after December 15, 2017. Early adoption is permitted. The Company is currently evaluating the impact that this new standard will have on its condensed consolidated financial statements and related disclosures.

2. DEBT

The table below summarizes the Company's debt outstanding at June 30, 2016 and December 31, 2015:

Debt Description	June 30, 2016	December 31, 2015	Maturity	Rate
Comerica Bank Loan and Security Agreement	$5,000,000	$5,000,000	June 2018	3.85%
Capital lease obligations - Noteholder lease	80,980	92,270	August 2019	8.00%
Capital lease obligations - office furniture	18,545	22,368	August 2018	9.80%
Convertible notes - related parties, net of discount of $1,392,671 and $2,010,743, respectively	36,531,560	33,363,488	November 2018	8.00%
Convertible notes, net of discount of $50,129	680,640	680,640	November 2018	8.00%
Total debt	42,311,725	39,158,766		
Less: current portion of long term debt				
Capital lease obligations	32,208	30,877		
Comerica Bank LSA	-	5,000,000		
Convertible notes - related parties, net of discount of $2,010,743	-	33,363,488		
Convertible notes, net of discount of $50,129	-	680,640		
Total current portion of long term debt	32,208	39,075,005		
Debt - long term	$42,279,517	$83,761		

Convertible Notes

During the six months ended June 30, 2016, the Company privately placed $2,550,000 in principal amount of additional unsecured Convertible Subordinated Notes (the “2014 NPA Notes”) to Union Bancaire Privée (“UBP”) under its existing unsecured Convertible Subordinated Note Purchase Agreement dated December 10, 2014 (the “2014 NPA”). The 2014 NPA Notes are convertible by the holder into shares of the Company’s common stock, par value $0.001 per share (the “Common Stock”) at a per share conversion price of $1.43.

On May 17, 2016, the Company and the holders of the majority of the aggregate outstanding principal amount of 2014 NPA Notes and holders of the majority of the aggregate outstanding principal amount of the Secured Promissory Notes (the “2007 NPA Notes”) issued under the Convertible Secured Subordinated Note Purchase Agreement dated November 14, 2007 (the "2007 NPA”) agreed to extend to November 14, 2018 the maturity date of the 2014 NPA Notes and the 2007 NPA Notes. Except as so extended, all of the terms relating to the outstanding 2007 Notes and the 2014 Notes continue in full force and effect. The Company is entitled to utilize the amounts available for future borrowing under each of the 2007 Note Purchase Agreement and the 2014 Note Purchase Agreement through November 14, 2018.

As a result of modification, any unamortized discount will be amortized into interest expense through the new maturity date of November 14, 2018.

The market value of the Company’s common stock on the date of each issuance of issuance of the 2014 NPA Notes to UBP was higher than the conversion price, which resulted in a beneficial conversion feature totaling $474,475 and corresponding debt discount, which is being amortized into interest expense through the maturity of the Notes.

The table below summarizes convertible notes issued as of June 30, 2016 by type:

Convertible Notes Type:	Balance
2007 NPA notes, net of discount	$29,428,736
2014 NPA notes, net of discount	7,783,464
Total convertible notes, net of discount	$37,212,200

Comerica LSA

On May 24, 2016, the Company and Comerica Bank entered into First Amendment to Loan and Security Agreement with Comerica Bank dated June 9, 2014, extending to June 6, 2018 the maturity date of the outstanding loan thereunder, which was originally scheduled to become due on June 6, 2016.

3. COMMITMENTS AND CONTINGENCIES

Aggregate future lease commitments

The Company leases computers, office equipment and office furniture under capital lease agreements that expire through August 2019. Total amount financed under these capital leases at June 30, 2016 was $99,525. This obligation is included within the Company's total debt.

The table below summarizes Company's future obligations under its capital leases:

Year:	
2016	$19,629
2017	39,259
2018	34,189
2019	19,412
	112,489
Less amount representing interest	(12,964)
Capital lease obligations	$99,525

The Company leases its office space in Raleigh, North Carolina pursuant to a lease with an initial term that expires in March 2019. The lease contains an option to renew for two additional three-year lease terms. In addition, the Company leaseda vehicle pursuant to a lease that expired in July 2016.

The table below summarizes the Company's future obligations under its office and vehicle operating leases:

Year:	
2016	$82,315
2017	167,786
2018	172,418
2019	44,082
Total	$466,601

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Legal Proceedings

From time to time, the Company may be subject to routine litigation, claims or disputes in the ordinary course of business. The Company defends itself vigorously in all such matters. In the opinion of management, no pending or known threatened claims, actions or proceedings against the Company are expected to have a material adverse effect on its financial position, results of operations or cash flows. However, the company cannot predict with certainty the outcome or effect of any such litigation or investigatory matters or any other pending litigations or claims. There can be no assurance as to the ultimate outcome of any such lawsuits and investigations. The Company will record a liability when it believes that it is both probable that a loss has been incurred and the amount can be reasonably estimated. The Company periodically evaluates developments in its legal matters that could affect the amount of liability that it has previously accrued, if any, and makes adjustments as appropriate. Significant judgment is required to determine both the likelihood of there being, and the estimated amount of, a loss related to such matters, and the Company's judgment may be incorrect. The outcome of any proceeding is not determinable in advance. Until the final resolution of any such matters that the Company may be required to accrue for, there may be an exposure to loss in excess of the amount accrued, and such amounts could be material.

4. EQUITY AND EQUITY BASED COMPENSATION

In May 2016, the Company's shareholders voted to increase the authorized shares of Common Stock from 45 million to 100 million shares. The increase became effective on June 7, 2016.

In May 2016, the Company's shareholders authorized adoption of the approved MobileSmith Inc. 2016 Equity Compensation Plan for officers, directors, employees and consultants, initially reserving for issuance thereunder 15,000,000 shares of Common Stock. As of June 30, 2016, no equity based compensation has been awarded under the 2016 Equity Compensation Plan.

The following is a summary of the stock option activity for the six months ended June 30, 2016:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding, December 31, 2015	361,349	$1.44		
Cancelled	(75,000)	1.50		
Issued	-	-		
Outstanding, June 30, 2016	286,349	1.42	2.37	$36,628
Vested and exercisable, June 30, 2016	234,014	$1.38	2.62	$34,894

Aggregate intrinsic value represents the difference between the closing price of the Company's common stock at June 30, 2016 and the exercise price of outstanding, in-the-money stock options. The closing price of the common stock at June 30, 2016, as reported on the Over-the-Counter Bulletin Board, was $1.40 per share.

At June 30, 2016, $18,735 unvested expense has yet to be recorded related to outstanding stock options.

5. MAJOR CUSTOMERS AND CONCENTRATION

For the six months ended June 30, 2016, one major customer accounted for 15% of total revenues and one customer accounted for 60% of the accounts receivable balance. For the six months ended June 30, 2015, two major customers accounted for 33% of total revenues and five customers accounted for 69% of the accounts receivable balance.

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

Information set forth in this Quarterly Report on Form 10-Q contains various forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act") and other laws. Forward-looking statements consist of, among other things, trend analyses, statements regarding future events, future financial performance, our plan to build our business and the related expenses, our anticipated growth, trends in our business, our ability to continue as a going concern, and the sufficiency of our capital resources including funds that we may be able to raise under our convertible note facility, our ability to raise financing from other sources and/or ability to defer expenditures, the impact of the liens on our assets securing amounts owed to third parties, expectation regarding competitors as more and larger companies attempt to market products/services competitive to our company, market acceptance of our new product offerings, including updates to our Platform, rate of new user subscriptions, market penetration of our products and expectations regarding our revenues and expense, all of which are based on current expectations, estimates, and forecasts, and the beliefs and assumptions of our management. Words such as "expect," "anticipate," "project," "intend," "plan," "estimate," variations of such words, and similar expressions also are intended to identify such forward-looking statements. These forward-looking statements are subject to risks, uncertainties, and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Readers are directed to risks and uncertainties identified under Part I, Item 1A, "Risk Factors," in the Annual Report on Form 10-K for the year ended December 31, 2015 and our subsequent periodic reports filed with the SEC for factors that may cause actual results to be different than those expressed in these forward-looking statements. Except as required by law, we undertake no obligation to revise or update publicly any forward-looking statements for any reason.

The following discussion is designed to provide a better understanding of our unaudited condensed consolidated financial statements, including a brief discussion of our business and products, key factors that impacted our performance, and a summary of our operating results. The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q, and the audited annual consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Annual Report. Historical results and percentage relationships among any amounts in the condensed consolidated financial statements are not necessarily indicative of trends in operating results for any future periods.

Overview

We develop and market a software-as-a-service ("SaaS") platform that allows non-programmers to design and build native mobile applications for smartphones and tablets. Our flagship product is the MobileSmith® Platform (the "Platform"). Platform related services often include data integration and training. We also provide consulting services, which include assistance with design and implementation of mobile strategy, implementation of mobile marketing strategy and the development of mobile apps. Revenue from such services is included in the Professional Services and Other Revenue line of our Statement of Operations. Delivery of Professional Services requires allocation of a portion of our research and development efforts into Cost of Revenue.

In our business model – the customers acquire access to the Platform through user subscription agreements and are able to obtain control of mobile app production. We often refer to our business model as platform-as-a-service ("PaaS"), because we not only offer cloud software to create mobile apps, we offer infrastructure to host the newly created mobile apps and back-office tools to manage those apps. Out Platform is a truly comprehensive offering and thus more accurately described by the PaaS model. In the industry and this report terms SaaS and PaaS may be used interchangeably as common reference to cloud computing model.

Our business model allows for creation and management of any desired number of apps by our customers for a monthly subscription fee. The on-demand PaaS model developed using multi-tenant architecture enables end users to visit a website and use the PaaS applications, all via a web browser, with no installation, no special information technology knowledge and no maintenance. The PaaS application is transformed into a service that can be used anytime and anywhere by the end user. Multi-tenant PaaS applications also permit us to add needed functionality to our applications in one location for the benefit of all end users. This capability allows us to provide upgrades universally.

During 2014, for the first time we installed our Platform in a local or a private cloud configuration for one of our government clients. Our Platform was safely placed behind the firewalls of a government department which would allow the organization to create and manage multiple mobile apps with targeted functionality for targeted audiences without going outside of the secure setting.

Target Market and Sales Channels

We believe that the do-it-yourself model for creation and management of apps will become a cost effective solution for enterprise clients who have an ever increasing need to interact with their customers and employees through mobile devices. Single apps may reach their limits of usability very quickly, if made complex. The Platform provides the subscriber with the capacity to create multiple, customized non-template apps with designated functionalities and specific designs without incurring additional costs.

Our market penetration strategy focuses on three distinct sectors:

Healthcare clients:

Healthcare organizations, such as hospitals and healthcare networks, follow departmental segmentation and focus on a specific territorial reach. Additionally, healthcare organizations are subject to increased regulation as a result of the Affordable Care Act and may be subject to penalties for delivering inefficient care under new Medicare regulations. Hospitals increasingly turn to portfolios of apps to increase efficiency and remain competitive. Outpatient care apps, wellness apps, physician referral apps, appointment apps, discharge apps, facility way-finding apps are just a few example areas where healthcare organizations are increasingly using app portfolios. We believe that the Platform has a significant competitive advantage in the healthcare space due to its ability to deliver a variety of targeted mobile solutions cost effectively.

Enterprise clients:

The second sector combines all other large and multi-national enterprise clients, where large-scale customization based on functionality or territory is of the highest value, and other contributors such as time to market, technology reach, and ease of use play important roles. These target clients may include large food chains, media and PR companies, software solutions providers, hardware manufacturers, mortgage brokers and real estate franchises.

Government:

We believe that the Platform has a unique capability to service various structures within federal, state and local governments, as government structure is highly segmented by function and territory. In addition, the Platform can be safely placed behind the firewalls of individual departments, where data security is a primary concern. Replicating the Platform and placing it behind a secure firewall would allow an organization to create and manage multiple mobile apps with targeted functionality for targeted audiences without going outside of the secure firewall.

RESULTS OF OPERATIONS

Comparison of the Three Months Ended June 30, 2016 (the “2016 Period”) to the Three Months Ended June 30, 2015 (the “2015 Period”).

	Three Months Ended June 30,		Increase (Decrease)	
	2016	2015	$	%
Revenue	498,323	407,545	90,778	22%
Cost of Revenue	144,227	88,501	55,726	63%
Gross Profit	354,096	319,044	35,052	11%
Sales and Marketing	325,450	267,047	58,403	22%
Research and Development	400,856	333,685	67,171	20%
General and Administrative	399,388	283,887	115,501	41%
Interest Expense	1,221,447	1,311,617	(90,170)	(7%)

Revenue increased by $90,778 or 22%. As the Platform evolves, we continue to add new features and extend our market penetration, expand our customer base and retain larger customers with broader range of needs in the mobile space who enter into more significant contracts for subscription revenue. Included in the total revenue in the 2015 Period was $30,000 of professional services revenue generated from one of our subscription clients. The professional services consisted of implementation of advanced Platform features, advanced data integration and mobile consulting. No such revenue was recognized during 2016 Period. We don’t expect professional services revenue to be a significant share of our total revenue in the future. Our revenues were impacted by one major contract for which revenue recognition has been deferred and has not yet started as of June 30, 2016 due to specifics of US GAAP (“United States Generally Accepted Accounting Principles”) revenue recognition requirements for sale of software products and services. Such deferred revenue was approximately $781,326, which comprised approximately 50% of the total deferred revenue balance. Once all revenue recognition criteria are met, the revenue will be recognized in accordance with our revenue recognition policy.

Cost of Revenue increased by $55,726 or 63%. The majority of the increase in cost of revenue is attributable to the growth of our Customer Success team, which expanded in the 2016 period, resulting in an increase in payroll and benefits of approximately $33,000. Additionally, cost of revenue included approximately $22,000 increase related to the delivery of professional services for mobile strategy and integration.

Gross Profit increased by $35,052 or 11%. Such increase is attributable to increased revenues due to a higher volume of clients and larger contract values, offset by the investment into Customer Success team to support the growth in revenue and costs associated with delivery of professional services revenue.

Sales and Marketing expense increased by $58,403 or 22%. An increase of approximately $24,000 is attributable to an acceleration of marketing campaigns and tradeshows as we identified a need to increase our exposure in the industry. General increase in travel for prospecting and client discovery was higher than the same period in 2015 by approximately $20,000. Outlays related to marketing related software and automation tools increase by approximately $8,000. Remainder of the increase was attributable to increase in sales and marketing payroll and other general marketing expenses.

Research and Development expense increased by $67,171 or 20%. This increase is attributable to an increase in payroll and related costs as a result of growth in our development and product teams, as well as increase in teams' general compensation levels as we continue to compete for top talent in a highly competitive labor market for software engineers and developers.

General and Administrative expense increased by $115,501 or 41% during the 2016 period. An increase of $83,000 is attributable to a non-cash reserve for doubtful accounts. An increase of $20,000 is attributable to a general increase in payroll and benefits, while the remaining increase is a combination of increases in travel, legal and compliance, and administrative costs.

Interest Expense decreased by $90,170 or 7%. The cash part of interest expense increased by approximately $100,000 due to the increase in the face value of our debt. The cash interest portion was offset by a decrease of approximately $190,000 in debt discount amortization as a result of the discount being amortized over additional two years due to the extension of the maturity date for our convertible debt..

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Comparison of the Six Months Ended June 30, 2016 (the "2016 Six Months Period") to the Six Months Ended June 30, 2015 (the "2015 Six Months Period").

	Six months ended June 30,		Increase (Decrease)	
	2016	2015	$	%
Revenue	969,453	833,733	135,720	16%
Cost of Revenue	264,611	157,243	107,368	68%
Gross Profit	704,842	676,490	28,352	4%
Sales and Marketing	561,174	559,246	1,928	0%
Research and Development	807,399	673,825	133,574	20%
General and Administrative	752,361	598,453	153,908	26%