

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 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, 2019**

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number: **001-38371**

**One Stop Systems, Inc.**

(Exact Name of Registrant as Specified in its Charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**33-0885351**  
(I.R.S. Employer  
Identification No.)

**2235 Enterprise Street #110**  
**Escondido, California 92029**  
(Address of principal executive offices including Zip Code)

**(877) 438-2724**  
(Registrant's telephone number, including area code)

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

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Trading symbol	Name of exchange on which registered
Common Stock, \$0.0001 par value per share	OSS	The Nasdaq Capital Market

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 such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input checked="" type="checkbox"/>

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

As of July 31, 2019, the registrant had 15,516,646 shares of common stock (par value \$0.0001) outstanding.

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## PART 1 – FINANCIAL INFORMATION

## Item 1. Financial Statements.

ONE STOP SYSTEMS, INC. (OSS)  
UNAUDITED CONSOLIDATED BALANCE SHEETS

	June 30, 2019	December 31, 2018
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 4,944,853	\$ 2,272,256
Accounts receivable, net	8,341,412	10,540,150
Inventories, net	8,859,281	6,823,930
Prepaid expenses and other current assets	778,629	666,330
	<u>22,924,175</u>	<u>20,302,666</u>
Property and equipment, net	2,840,239	1,759,086
Deposits and other	42,088	49,966
Deferred tax assets, net	3,050,854	2,505,632
Goodwill	7,120,510	7,914,211
Intangible assets, net	1,711,687	3,525,257
	<u>\$ 37,689,553</u>	<u>\$ 36,056,818</u>

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED BALANCE SHEETS - CONTINUED**

	June 30, 2019	December 31, 2018
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities		
Accounts payable	\$ 3,143,232	\$ 3,708,865
Accrued expenses and other liabilities	6,017,251	3,930,718
Borrowings on bank lines of credit (Note 8)	1,062,352	422,960
Current portion of notes payable, net of debt discount of \$7,019 and \$0, respectively (Note 8)	1,729,369	1,156,915
Current portion of related-party notes payable, net of debt discount of \$23,061 and \$0, respectively (Note 8)	534,084	-
Total current liabilities	12,486,288	9,219,458
Notes payable, net of current portion and debt discount of \$5,556 and \$0, respectively (Note 8)	387,066	265,038
Related-party notes payable, net of current portion and debt discount of \$18,256 and \$0, respectively (Note 8)	487,595	-
Total liabilities	13,360,949	9,484,496
Commitments and contingencies (Note 11)		
Stockholders' equity		
Common stock, \$.0001 par value; 50,000,000 shares authorized; 14,497,647 and 14,216,328 shares issued and outstanding, respectively	1,450	1,422
Additional paid-in capital	27,717,796	27,424,113
Noncontrolling interest	500	500
Accumulated other comprehensive income	3,076	1,142
Accumulated deficit	(3,394,218)	(854,855)
Total stockholders' equity	24,328,604	26,572,322
	<u>\$ 37,689,553</u>	<u>\$ 36,056,818</u>

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS**

	For The Three Months Ended June 30,		For The Six Months Ended June 30,	
	2019	2018	2019	2018
Revenue	\$ 14,886,236	\$ 5,892,666	\$ 24,944,135	\$ 13,012,378
Cost of revenue	9,473,078	4,252,484	17,119,354	9,159,330
Gross margin	5,413,158	1,640,182	7,824,781	3,853,048
Operating expenses:				
General and administrative	3,931,478	1,097,552	5,975,413	2,170,600
Marketing and selling	1,237,003	702,474	2,374,936	1,571,489
Research and development	1,225,157	958,775	2,487,121	1,931,406
Total operating expenses	6,393,638	2,758,801	10,837,470	5,673,495
Loss from operations	(980,480)	(1,118,619)	(3,012,689)	(1,820,447)
Other income (expense):				
Interest expense	(53,013)	-	(59,281)	(55,661)
Other, net	(3,068)	54,430	(11,232)	122,039
Total other (expense) income, net	(56,081)	54,430	(70,513)	66,378
Loss before income taxes	(1,036,561)	(1,064,189)	(3,083,202)	(1,754,069)
Provision (benefit) for income taxes	558,072	555,629	(543,839)	772,752
Net loss	\$ (1,594,633)	\$ (1,619,818)	\$ (2,539,363)	\$ (2,526,821)
Net loss attributable to noncontrolling interest	\$ -	\$ (116,996)	\$ -	\$ (229,581)
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)
Net loss per share attributable to common stockholders:				
Basic	\$ (0.11)	\$ (0.12)	\$ (0.18)	\$ (0.20)
Diluted	\$ (0.11)	\$ (0.12)	\$ (0.18)	\$ (0.20)
Weighted average common shares outstanding:				
Basic	14,442,291	12,773,419	14,341,560	11,464,246
Diluted	14,442,291	12,773,419	14,341,560	11,464,246

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**

	For The Three Month Periods ended June 30,		For The Six Month Periods ended June 30,	
	2019	2018	2019	2018
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)
Other comprehensive income				
Change in foreign currency translation adjustment	43,803	-	1,934	-
Total other comprehensive income	43,803	-	1,934	-
Comprehensive loss	<u>\$ (1,550,830)</u>	<u>\$ (1,502,822)</u>	<u>\$ (2,537,429)</u>	<u>\$ (2,297,240)</u>

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**For The Three and Six Month Periods ended June 30, 2019**

	Series C Preferred Stock		Series B Preferred Stock		Series A Preferred Stock		Common Stock		Additional	Noncontrolling Interest	Accumulated Other	Accumulated Deficit	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Paid-in-Capital		Income		
Balance, January 1, 2019	-	\$ -	-	\$ -	-	\$ -	14,216,328	\$ 1,422	\$ 27,424,113	\$ 500	\$ 1,142	\$ (854,855)	\$ 26,572,322
Stock-based compensation	-	-	-	-	-	-	-	-	167,474	-	-	-	167,474
Exercise of stock options, RSU's and Warrants	-	-	-	-	-	-	54,098	5	14,196	-	-	-	14,201
Currency translation adjustment	-	-	-	-	-	-	-	-	-	-	(41,869)	-	(41,869)
Net loss	-	-	-	-	-	-	-	-	-	-	-	(944,730)	(944,730)
Balance, March 31, 2019	-	\$ -	-	\$ -	-	\$ -	14,270,426	1,427	\$ 27,605,783	\$ 500	\$ (40,727)	\$ (1,799,585)	\$ 25,767,398
Stock-based compensation	-	-	-	-	-	-	-	-	157,809	-	-	-	157,809
Relative fair value of warrants issued with notes payable and notes payable to related parties	-	-	-	-	-	-	-	-	60,158	-	-	-	60,158
Exercise of stock options, RSU's and Warrants	-	-	-	-	-	-	227,221	23	6,925	-	-	-	6,948
Taxes paid on net issuance of employee stock options	-	-	-	-	-	-	-	-	(112,879)	-	-	-	(112,879)
Currency translation adjustment	-	-	-	-	-	-	-	-	-	-	43,803	-	43,803
Net loss	-	-	-	-	-	-	-	-	-	-	-	(1,594,633)	(1,594,633)
Balance, June 30, 2019	-	\$ -	-	\$ -	-	\$ -	14,497,647	1,450	\$ 27,717,796	\$ 500	\$ 3,076	\$ (3,394,218)	\$ 24,328,604

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY - CONTINUED**  
**For The Three and Six Month Periods ended June 30, 2018**

	Series C Preferred Stock		Series B Preferred Stock		Series A Preferred Stock		Common Stock		Additional	Noncontrolling Interest	Accumulated Other	Accumulated Deficit	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Paid-in-Capital		Comprehensive Income		
Balance, January 1, 2018	1,087,006	\$ 1,604,101	1,450,000	\$ 697,996	500,000	\$ 114,430	5,514,917	\$ 551	\$ 3,484,428	\$ 436,842	\$ -	\$ 281,423	\$ 6,619,771
Conversion of preferred stock to common stock upon initial public offering	(1,087,006)	(1,604,101)	(1,450,000)	(697,996)	(500,000)	(114,430)	3,037,006	304	2,416,223	-	-	-	-
Stock-based compensation	-	-	-	-	-	-	-	-	35,318	-	-	-	35,318
Exercise of stock options	-	-	-	-	-	-	321,366	32	54,543	-	-	-	54,575
Taxes paid on net issuance of employee stock options	-	-	-	-	-	-	-	-	(274,663)	-	-	-	(274,663)
Relative fair value of warrants issued to Underwriters with IPO	-	-	-	-	-	-	-	-	669,408	-	-	-	669,408
Proceeds from issuance of stock, net of issuance costs of \$3,367,760	-	-	-	-	-	-	3,900,000	390	16,131,850	-	-	-	16,132,240
Noncontrolling interest in consolidated subsidiary (Note 1)	-	-	-	-	-	-	-	-	-	(112,585)	-	-	(112,585)
Net loss	-	-	-	-	-	-	-	-	-	-	-	(794,418)	(794,418)
Balance, March 31, 2018	-	\$ -	-	\$ -	-	\$ -	12,773,289	\$ 1,277	\$ 22,517,107	\$ 324,257	\$ -	\$ (512,995)	\$ 22,329,646
Stock-based compensation	-	-	-	-	-	-	-	-	124,815	-	-	-	124,815
Exercise of stock options	-	-	-	-	-	-	5,921	1	4,574	-	-	-	4,575
Noncontrolling interest in consolidated subsidiary (Note 1)	-	-	-	-	-	-	-	-	-	(116,996)	-	-	(116,996)
Net loss	-	-	-	-	-	-	-	-	-	-	-	(1,502,822)	(1,502,822)
Balance, June 30, 2018	-	\$ -	-	\$ -	-	\$ -	12,779,210	1,278	\$ 22,646,496	\$ 207,261	\$ -	\$ (2,015,817)	\$ 20,839,218

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	For The Six Months Ended June 30,	
	2019	2018
<b>Cash flows from operating activities:</b>		
Net loss	\$ (2,539,363 )	\$ (2,526,821 )
Net loss attributable to noncontrolling interest	-	(229,581 )
Net loss attributable to common stockholders	(2,539,363 )	(2,297,240 )
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Net loss attributable to noncontrolling interest	-	(229,581 )
Deferred (benefit) provision for income taxes	(544,404 )	788,226
Unrealized gain on foreign currency transactions	18,743	-
(Gain) on disposal of property and equipment	(63,939 )	-
Provision for bad debt	1,358	94,431
Impairment of goodwill	1,988,701	-
Warranty reserves	4,818	(2,916 )
Amortization of deferred gain	(32,957 )	(57,675 )
Depreciation and amortization	886,982	528,494
Inventory reserves	136,609	244,399
Amortization of debt discount	6,266	24,830
Stock-based compensation expense	325,283	160,133
Changes in operating assets and liabilities:		
Accounts receivable	2,185,438	587,587
Inventories	(2,118,771 )	(349,512 )
Prepaid expenses and other current assets	(106,591 )	(325,450 )
Accounts payable	(559,831 )	(2,631,811 )
Accrued expenses and other liabilities	2,125,542	(382,004 )
Net cash provided by (used in) operating activities	<u>1,713,884</u>	<u>(3,848,089)</u>
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment, including capitalization of labor costs for test equipment and ERP, (net)	(1,356,975 )	(60,210 )
Proceeds from sales of property and equipment	1,050	-
Net cash used in investing activities	<u>(1,355,925)</u>	<u>(60,210)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from stock options exercised	21,149	59,150
Payment of payroll taxes on net issuance of employee stock options	(112,879 )	(274,663 )
Stock issuance costs	-	(1,810,902 )
Proceeds from issuance of common stock	-	19,500,000
Net borrowings (repayments) on bank lines of credit	1,028,134	(3,334,508 )
Net borrowings (repayments) on related-party notes payable	932,762	(163,483 )
Net borrowings (repayments) on notes payable	454,004	(985,692 )
Net cash provided by financing activities	<u>2,323,170</u>	<u>12,989,902</u>
Net change in cash and cash equivalents	2,681,129	9,081,603
Effect of exchange rates on cash	(8,532 )	-
Cash and cash equivalents, beginning of period	2,272,256	185,717
Cash and cash equivalents, end of period	<u>\$ 4,944,853</u>	<u>\$ 9,267,320</u>

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED**

	For The Six Months Ended June 30,	
	2019	2018
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid during the period for interest	\$ 59,281	\$ 39,351
Cash paid during the period for income taxes	\$ 4,000	\$ -
<b>Supplemental disclosure of non-cash transactions:</b>		
Relative fair value of warrants issued in connection with initial public offering	\$ -	\$ 669,408
Relative fair value of warrants issued in connection with notes and related-party notes payable	\$ 60,158	\$ -
Reclassification of prepaid IPO expenses to additional paid in capital	\$ -	\$ 887,450
Reclassification of inventories to property and equipment	\$ 67,948	\$ 445,366

*See accompanying notes to consolidated financial statements*

**ONE STOP SYSTEMS, INC. (OSS)**  
**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**  
**For The Six Months Periods Ended June 30, 2019 and 2018**

**NOTE 1 – THE COMPANY AND BASIS OF PRESENTATION**

**Nature of Operations**

One Stop Systems, Inc. (“we,” “our,” “OSS,” or the “Company”) was originally incorporated as a California corporation in 1999 after initially being formed as a California limited liability company in 1998. On December 14, 2017, the Company was reincorporated as a Delaware corporation in connection with its initial public offering. The Company designs, manufactures and markets industrial grade computer systems and components that are based on industry standard computer architectures. The Company markets its products to manufacturers of automated equipment used for telecommunications, industrial and military applications.

During the year ended December 31, 2015, the Company formed a new wholly-owned subsidiary in Germany (“OSS GmbH”). During July 2016, the Company acquired Mission Technologies Group, Inc. (“Magma”) and its operations.

In April 2017, the Company and a related entity formed a joint venture named SkyScale, LLC in the State of California (“SkyScale”). In accordance with the Contribution Agreement, each member contributed \$750,000 and received a 50% interest in the joint venture. The purpose of SkyScale was to engage in the business of providing high performance computing capabilities as cloud services.

On December 31, 2018, as a result of changes in the competitive landscape and downward pressure on pricing from large competitors, the members to the SkyScale joint venture agreement agreed to dissolve SkyScale. As a result, it became necessary for OSS to write-off the outstanding balances of accounts and notes receivable and interest in the amount of \$648,411, which write-off was offset by receipt of equipment valued at \$160,000 and allocation of income from disposition of assets and liabilities of \$71,502. Additional reserves for future expenses to be incurred in the process of closing SkyScale were recorded in the amount of \$288,400. As a result of the above, total charges related to the dissolution of SkyScale were \$705,309 during the year ended December 31, 2018.

In May 2017, the Company entered into a Technology and Software License Agreement with Western Digital (“WDT”) for their Ion flash storage software. The agreement provides the Company with the Ion source code and rights to develop and market derivative products. The Company intends to develop and sell Ion flash storage software with its high-density storage arrays, as well as service existing WDT software users (Note 3).

Also, in July 2017, the Company entered in to a Service Agreement with WDT to service its existing customer base that utilizes Ion flash storage software. The Company also purchased certain equipment from WDT and hired selected employees to assist in the servicing of these existing customers. Management has determined that the activities and assets acquired from WDT comprise a business as defined in ASC 805-10-55-4 through 55. Consideration paid by the Company to WDT pursuant to the arrangements described above was \$67,000. In addition, the Company is required to pay prospective royalties to WDT of \$2,500 or \$5,000 for each sale of the Company’s products that include licensed software. WDT is obligated to pay the Company for services rendered to support existing WDT software users the amount of \$1,400,000 in defined declining quarterly amounts over a three year period. Management does not believe this business acquisition meets the significance definition provided in Regulation S-X, Rule 210.1-02(w).

On August 31, 2018, the Company acquired Concept Development Inc. (CDI) located in Irvine, California for cash of \$646,759, and common stock valued at \$4,194,673 (Note 3). CDI specializes in the design and manufacture of custom high-performance computing systems for airborne in-flight entertainment systems.

On October 31, 2018, the Company's wholly-owned German subsidiary, OSS GmbH, acquired 100% of the outstanding stock of Bressner Technology GmbH, a Germany limited liability company located near Munich, Germany, from its principal owners for cash consideration of €4,725,000 (US\$5,374,582) and stock consideration of 106,463 newly-issued restricted shares of the Company's common stock.

#### Going Concern Considerations

On February 1, 2018, the Company completed its initial public offering through the initial sale of 3,800,000 shares of common stock at a price to the public of \$5.00 per share (see Note 9). Proceeds from the sale were used to retire outstanding debt obligations, complete complimentary business acquisitions, and provide the Company with working capital.

The combination of continued revenue and gross profit growth, has resulted in growth of the organization as a whole, along with acquisitions of two companies, but has been offset by increased spending in all areas of operating expenses: general & administrative, marketing & selling, along with research & development. The Company is developing plans for cost containment, as well as debt and/or equity financing to ensure that liquidity will be sufficient to meet our cash requirements for current operations through at least a period of the next twelve months.

As of March 20, 2019, the Company received funding commitments in the amount of \$4,000,000 from members of the Board of Directors, of which \$1,500,000 has been borrowed from multiple parties as of June 30, 2019.

On May 15, 2019, the Company filed an S-3 prospectus with the Securities and Exchange Commission which became effective on June 19, 2019, and allows the Company to offer up to \$100,000,000 aggregate dollar amount of shares of its common stock or preferred stock, debt securities, warrants to purchase its common stock, preferred stock or debt securities, subscription rights to purchase its common stock, preferred stock or debt securities and/or units consisting of some or all of these securities, in any combination, together or separately, in one or more offerings, in amounts, at prices and on the terms that the Company will determine at the time of the offering and which will be set forth in a prospectus supplement and any related free writing prospectus.

On June 26, 2019, the Company filed a prospectus supplement relating to its common stock, par value \$0.0001 per share, whereby under the prospectus supplement the Company may offer and sell common stock having an aggregate offering price of up to \$10,000,000 through Noble Capital Markets, Inc., ("Noble"), acting as the Company's agent. As such, the Company entered into an Equity Distribution Agreement with Noble dated as of June 26, 2019. As of July 31, 2019, the Company has sold 1,019,561 shares of common stock through this offering for total gross proceeds of \$1,773,332, which resulted in net proceeds to us of \$1,746,046, after deducting compensation payable to Noble of \$27,286.

As a result, management believes that the Company has sufficient liquidity to satisfy its anticipated cash requirements for at least the next twelve months. However, there can be no assurance that our operations will become profitable or that external sources of financing, including the issuance of debt and/or equity securities, will be available at times and on terms acceptable to us, or at all. The Company's management prepares budgets and monitors the financial results of the Company as a tool to align liquidity needs to the recurring business requirements.

#### Basis of Presentation

The accompanying financial statements have been prepared on an accrual basis of accounting in accordance with United States Generally Accepted Accounting Principles ("U.S. GAAP"), as set forth in the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC").

The unaudited consolidated financial statements herein have been prepared by the Company pursuant to the rules and regulations of the United States Securities Exchange Commission ("SEC"). The accompanying interim unaudited financial statements have been prepared under the presumption that users of the interim financial information have either read or have access to the audited consolidated financial statements for the latest year ended December 31, 2018. Accordingly, note disclosures which would substantially duplicate the disclosures contained in the December 31, 2018 audited consolidated financial statements have been omitted from these interim unaudited

consolidated financial statements. The Company evaluated all subsequent events and transactions through the date of filing this report.

Certain information and note disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2019, are not necessarily indicative of the results that may be expected for the year ending December 31, 2019. For further information, refer to the audited consolidated financial statements and notes for the year ended December 31, 2018 included in the Company's Annual Report on Form 10-K filed with the SEC on March 21, 2019.

Principles of Consolidation

The accompanying unaudited consolidated financial statements include the accounts of OSS, which include the results from the Magma acquisition, Ion business combination, and acquisition of Concept Development Inc., since their respective dates of acquisition, its wholly-owned subsidiary, OSS GmbH, which includes the acquisition of Bressner Technology GmbH on October 31, 2018 and the accounts of the joint venture, SkyScale LLC, which was approved for dissolution on December 31, 2018 (collectively referred to as the "Company"). Intercompany balances and transactions have been eliminated in consolidation.

The assets and liabilities of SkyScale are as follows:

	June 30, 2019	December 31, 2018
Cash and cash equivalents	\$ -	\$ 47,663
Receivables	-	-
Other assets	-	-
Fixed assets	-	-
Total assets	\$ -	\$ 47,663
Accounts payable	\$ -	\$ 46,663
Accrued expenses	-	-
Notes payable	-	-
Total liabilities	-	46,663
Members' equity	-	1,000
Total liabilities and members' equity	\$ -	\$ 47,663

Operating results for SkyScale are as follows:

	For The Six Months Ended June 30,	
	2019	2018
Net revenue	\$ -	\$ 120,539
Cost of revenue	-	148,961
Gross margin	-	(28,422)
Operating expenses:		
General and administrative	-	158,013
Marketing and selling	-	40,716
Total operating expenses	-	198,729
Loss from operations	-	(227,151)
Other (expense) income	-	1,981
Net loss	\$ -	\$ (225,170)

The non-controlling interest attributable to SkyScale is shown as a component of equity on the consolidated balance sheets and the share of the loss attributable to the non-controlling interest is shown as a component of income (loss) in the accompanying consolidated statements of operations. Management determined that the dissolution of SkyScale did not represent a strategic shift that has a major effect on the Company's operations and financial results. Accordingly, it has not been reported as discontinued operations.

## **NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES**

### **Use of Estimates**

The preparation of consolidated 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, liabilities, revenues and expenses, and disclosures of contingent assets, liabilities, and expenses at the date of the consolidated financial statements during the reporting period.

Significant estimates made by management include, among others, the fair value of acquired net assets of CDI in August 2018, and Bressner Technology GmbH in October 2018, dissolution expenses for SkyScale, the allowance for doubtful accounts, fair value of stock options, recoverability of inventories and long-lived assets, and realizability of deferred tax assets. Actual results could differ from those estimates.

### **Concentration Risks**

At times, deposits held with financial institutions may exceed the amount of insurance provided by the Federal Deposit Insurance Corporation ("FDIC"), which provides basic deposit coverage with limits up to \$250,000 per owner. As of June 30, 2019, the Company had \$4,062,257 in excess of the insurance limits. The Company has not experienced any such losses in these accounts. In Germany, the deposit insurance is €100,000 per bank, per customer. As of June 30, 2019, Bressner has €236,412 (US\$268,798) on deposit with banks in excess of the insurance limits.

In the three month periods ended June 30, 2019 and 2018, our top three customers represented approximately 52%, and 48% of sales, respectively, and approximately 44%, and 49% for the six month periods ended June 30, 2019 and 2018, respectively. As of June 30, 2019 and December 31, 2018, three customers accounted for 57% and 64% of net trade accounts receivables, respectively.

The Company made purchases from three suppliers which represented approximately 20% and 48% of purchases for the three month periods ended June 30, 2019 and 2018, respectively, and approximately 29% and 45% for the six month periods ended June 30, 2019 and 2018, respectively.

### **Cash and Cash Equivalents**

Cash and cash equivalents consist of cash on deposit and money market accounts. The Company considers all highly liquid temporary cash investments with an initial maturity of six months or less when acquired to be cash equivalents. Management believes that the carrying amounts of cash equivalents approximate their fair value because of the short maturity period.

### **Accounts Receivable**

Accounts receivable are presented at net realizable value. This value includes an appropriate allowance for estimated uncollectible accounts to reflect any loss anticipated on the trade accounts receivable and unbilled receivables. Unbilled receivables include costs and gross profit earned in excess of billings. The allowance for doubtful accounts is an estimate to cover the losses resulting from the inability of customers to make payments on their outstanding balances and unbilled receivables. In estimating the required allowance, management considers the overall quality and aging of the accounts receivable, specific customer circumstances, current economic trends, and historical experience with collections. At June 30, 2019 and December 31, 2018, the allowance for doubtful accounts was \$14,727 and \$13,403, respectively.

Revenues earned in excess of related billings are recorded as an asset on the balance sheet as unbilled receivables. Unbilled receivables as of June 30, 2019 and December 31, 2018, were \$81,826 and \$65,127, respectively.

#### Inventories

Inventories are valued at the lower of cost or net realizable value determined on a first-in, first-out basis. The Company uses the average cost method for purposes of determining cost, which approximates the first-in, first-out method.

The Company establishes reserves on its inventories to write-down the carrying value of its estimated obsolete or excess inventories to estimated net realizable value based upon observations of historical usage and assumptions about future demand and market conditions. In addition, the Company considers changes in the market value of components in determining the net realizable value of its inventory. Inventory reserves are not typically reversed until the specific inventories are sold or otherwise disposed.

Actual demand, product mix and alternative usage may be lower than those that we project and this difference could have a material adverse effect on our gross margin if inventory write-downs beyond those initially recorded become necessary. Alternatively, if actual demand, product mix and alternative usage are more favorable than those we estimated at the time of such a write-down, our gross margin could be favorably impacted in future periods.

#### Property and Equipment

Property and equipment, other than leasehold improvements, are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the assets, generally from three to five years. Leasehold improvements are recorded at cost and are amortized using the straight-line method over the shorter of the remaining lease term or the estimated useful life of the related asset. Tooling and test equipment includes capitalized labor costs associated with the development of the related tooling and test equipment. Costs incurred for maintenance and repairs are expensed as incurred, and expenditures for major replacements and improvements are capitalized. Upon retirement or sale, the cost and related accumulated depreciation and amortization of disposed assets are removed from the accounts and any resulting gain or loss is included in other expense, net.

#### Goodwill

Goodwill represents the excess of the purchase price paid over the fair value of the net assets acquired in business combinations. Goodwill is not amortized but is tested for impairment at least annually or when we deem that a triggering event has occurred. The Company reviews goodwill for impairment annually on December 31<sup>st</sup>. The Company completed its annual assessment for goodwill impairment and determined that goodwill is not impaired as of December 31, 2018 and no adjustment was required.

During the six month period ended June 30, 2019, the Company performed a goodwill impairment test of goodwill and as a result of a short-fall in the actual overall financial performance of CDI as compared to plan, a recurring need for working capital, and a decrease in the Company's stock price. As a result of this interim evaluation, the Company recorded an impairment loss to goodwill of \$1,988,701 which was charged to operating expenses in the current period. During the year ended December 31, 2018, the Company recognized goodwill related to two business acquisitions as described in Note 3.

#### Intangible Assets and Long-lived Assets

We evaluate our intangible and long-lived assets for impairment when events or circumstances arise that indicate our intangible and long-lived assets may be impaired. Indicators of impairment include, but are not limited to, a significant deterioration in overall economic conditions, a decline in our market capitalization, the loss of significant business, significant decreases in funding for our contracts, or other significant adverse changes in industry or market conditions. The Company completed its qualitative assessment for impairment in December 2018 and determined that there was no impairment as of December 31, 2018. There were no events or circumstances that arose during the six month period ended June 30, 2019, that gave an indication of impairment, except as discussed in Note 3. There can be no assurance, however, that market conditions will not change or demand for the Company's products will continue, which could result in an impairment of intangible and long-lived assets in the future.

## Revenue Recognition

On January 1, 2019, the Company adopted the new accounting standard update ASC 606, Revenue from Contracts with Customers, which superseded nearly all existing revenue recognition guidance under GAAP, to all contracts using the modified retrospective method. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The Company's performance obligations are satisfied over time as work is performed or at a point in time. The majority of the Company's revenue is recognized at a point in time when products ship and control is transferred to the customer. The Company determines revenue recognition through the following steps: (1) identification of the contract with a customer; (2) identification of the performance obligations in the contract; (3) determination of the transaction price; (4) allocation of the transaction price to the performance obligations in the contract; and (5) recognition of revenue when, or as, a performance obligation is satisfied.

The Company's contracts are executed through a combination of written agreements along with purchase orders with all customers including certain general terms and conditions. Generally, purchase orders entail products, quantities and prices, which define the performance obligations of each party and are approved and accepted by the Company. The Company's contracts with customers do not include extended payment terms. Payment terms vary by contract type and type of customer and generally range from 30 to 60 days from invoice. Additionally, taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by the Company from a customer and deposited with the relevant government authority, are excluded from revenue.

The transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring goods or services to the customer adjusted for estimated variable consideration, if any. Variable consideration may include discounts, rights of return, refunds, and other similar obligations. The Company allocates the transaction price to each distinct product and service based on its relative standalone selling price. The standalone selling price for products primarily involves the cost to produce the deliverable plus the anticipated margin and for services is estimated based on the Company's approved list price.

In the normal course of business, the Company does not accept product returns unless the items are defective as manufactured. The Company establishes provisions for estimated returns and warranties. In addition, the Company does not typically provide customers with the right to a refund and does not transact for noncash consideration.

Customer agreements include one vendor managed inventory program. The Company recognizes revenue under this arrangement when (i) risks of ownership have passed to the customer; (ii) the customer's commitment to purchase the goods is fixed; (iii) there is a fixed schedule for delivery of the goods that is reasonable and consistent with the customer's business purpose; (iv) the Company does not have any specific performance obligations such that the earning process is not complete; (v) the ordered goods have been segregated from the Company's inventory and are not subject to being used to fill other orders; and (vi) the product is complete and ready for shipment. Also, such arrangement must be requested by the customer and the customer has explained a substantial business purpose for the arrangement. Management also considers whether the customer's custodial risks are insured and whether modifications to the Company's normal billing and credit terms were required.

The Company recorded revenue from product sales that are held in vendor managed inventory under these agreements of \$3,674,366 and \$1,923,450, for the three month periods ended June 30, 2019 and 2018, respectively, and \$5,168,444 and \$2,913,851, for the six month periods ended June 30, 2019 and 2018, respectively.

Revenues on certain fixed-price contracts where we provide engineering services, prototypes and completed products are recognized over the contract term based on the percentage of completion or based upon milestones delivered that are provided during the period and compared to the total estimated development and milestone goals to be provided over the entire contract. These services require that we perform significant, extensive and complex design, development, modification or implementation of our customers' systems. Performance will often extend over long periods of time, and our right to receive future payment depends on our future performance in accordance with the agreement. Recognized revenue using the percentage of completion accounting method was \$166,573 and \$0 during the three month periods ended June 30, 2019 and 2018, respectively, and \$201,053 and \$0 during the six month periods ended June 30, 2019 and 2018, respectively.

The percentage-of-completion methodology involves recognizing probable and reasonably estimable revenue using the percentage of services completed, on a current cumulative cost to estimate total cost basis, using a reasonably consistent profit margin over the period. Due to the long-term nature of these projects, developing the estimates of costs often requires significant judgment. Factors that must be considered in estimating the progress of work completed and ultimate cost of the projects include, but are not limited to, the availability of labor and labor productivity, the nature and complexity of the work to be performed and the impact of delayed performance. If changes occur in delivery, productivity or other factors used in developing the estimates of costs or revenues, we revise our cost and revenue estimates, which may result in increases or decreases in revenues and costs, and such revisions are reflected in earnings in the period in which the revision becomes known.

Related billings that are in excess of revenue earned are deferred and recorded as a liability on the balance sheet until the related services are provided. Deferred revenue was \$49,436 and \$133,995 as of June 30, 2019 and December 31, 2018, respectively. The Company recognizes revenues for non-refundable, upfront implementation fees on a straight-line basis over the period beginning with initiation of ongoing services through the end of the contract term.

The Company's operating segment revenues disaggregated by primary geographic market, which is determined based on a customer's geographic location, for the three and six month period ended June 30, 2019 is as follows:

Entity:	For The Three Month Period ended June 30, 2019			For The Six Month Period ended June 30, 2019		
	Domestic	International	Total	Domestic	International	Total
Customized computers and flash arrays	\$ 5,109,661	\$ 4,898,143	\$ 10,007,804	\$ 7,152,171	\$ 8,085,719	\$ 15,237,890
In-flight entertainment & connectivity	881,062	13,500	894,562	1,177,591	16,425	1,194,016
Value-added reseller with minimal customization	27,851	3,956,019	3,983,870	520,830	7,991,399	8,512,229
	<u>\$ 6,018,574</u>	<u>\$ 8,867,662</u>	<u>\$ 14,886,236</u>	<u>\$ 8,850,592</u>	<u>\$ 16,093,543</u>	<u>\$ 24,944,135</u>

During the comparative 2018 periods, the Company only had one operating segment.

#### Warranty Reserve

The Company offers product warranties that extend for one year from the date of sale. Such warranties require the Company to repair or replace defective product returned to the Company during the warranty period at no cost to the customer. The Company records an estimate for warranty-related costs at the time of sale based on its historical and estimated future product return rates and expected repair or replacement costs (Note 7).

While such costs have historically been within management's expectations and the provisions established, unexpected changes in failure rates could have a material adverse impact on the Company, requiring additional warranty reserves and could adversely affect the Company's gross profit and gross margins.

The Company offers customers extended warranties beyond the standard one-year warranty on the product. The customer can purchase extended warranties from one to five years, in the bronze, silver or gold categories. This entails hardware repair or replacement, shipping methods on how the warranties will be returned / delivered, response times and hours of operations to receive support. The amount of warranties sold for the three and six months periods ended June 30, 2019 and 2018 was \$7,014 and \$93,941 and \$87,137 and \$110,125, respectively.

The revenue that was recognized for the warranties sold for the three months periods ended June 30, 2019 and 2018 was \$104,474 and \$31,747, respectively, and \$211,172 and \$59,195 for the six months periods ended June 30, 2019 and 2018, respectively. The Company does have recourse with some of its suppliers that offer more than a one-year guarantee on parts, but this is not standard. The few that offer greater than a year warranty, the Company may be able to cover the cost of the part from the manufacturer for the failed part. The amounts of these costs vary in a wide range, but are not material, due to the infrequency of failure. The amount of liability on the Company's books for revenue not recognized as of June 30, 2019 and December 31, 2018 were \$285,298 and \$409,334, respectively.

### Shipping and Handling Costs

The Company's shipping and handling costs are included in cost of goods sold for all periods presented.

### Foreign Currency

We operate primarily in the United States. Foreign sales of products and services are primarily denominated in U.S. dollars. We also conduct limited business outside the United States through our foreign subsidiary in Germany, where business is largely transacted in non-U.S. dollar currencies, particularly the Euro, which is subject to fluctuations due to changes in foreign currency exchange rates. Accordingly, we are subject to exposure from changes in the exchange rates of local currencies. Foreign currency transaction gains and losses are recorded in other income (expense), net in the consolidated statements of operations.

OSS GmbH operates as an extension of OSS's domestic operations. The functional currency of OSS GmbH is the Euro. Transactions denominated in currencies other than the functional currency are remeasured to the functional currency at the average exchange rate in effect during the period. At the end of each reporting period, monetary assets and liabilities are remeasured using exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are remeasured at historical exchange rates. Consequently, changes in the exchange rates of the currencies may impact the translation of the foreign subsidiaries' statements of operations into U.S. dollars, which may in turn affect our consolidated statements of operations. The resulting foreign currency translation adjustments are recorded as a separate component of accumulated other comprehensive income in the consolidated balance sheet.

### Derivative Financial Instruments

We employ derivatives to manage certain market risks through the use of foreign exchange forward contracts. We do not use derivatives for trading or speculative purposes. Our derivatives are designated as a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). We hedge a portion of the exchange risk involved in anticipation of highly probable foreign currency-denominated transactions. In anticipation of these transactions, we enter into foreign exchange contracts to provide currency at a fixed rate. As of June 30, 2019, the Company had no foreign exchange contracts outstanding.

Unrealized gains on derivatives designated as cash flow hedges are recorded at fair value as assets, and unrealized losses on derivatives designated as cash flow hedges are recorded at fair value as liabilities. For derivative instruments designated as cash flow hedges, the effective portion is reported as a component of accumulated other comprehensive income until reclassified into interest expense in the same period the hedged transaction affects earnings. The gain or loss on the ineffective portion is recognized as "Other income (expense) – net" in the consolidated statements of income in each period.

### Stock-Based Compensation

The Company accounts for employee and director share-based compensation in accordance with the provisions of ASC Topic 718 "*Compensation – Stock Compensation*". Under ASC 718, share-based compensation cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity grant).

All transactions in which goods or services are the consideration received for the issuance of equity instruments to non-employees are accounted for based on the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more reliably measurable. The measurement date used to determine the estimated fair value of the equity instrument issued is the earlier of the date on which the third-party performance is complete or the date on which it is probable that performance will occur.

Employee and director 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 during the period. Given that stock-based compensation expense recognized in the accompanying consolidated statements of operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The Company's estimated average forfeiture rates are based on historical forfeiture experience and estimated future forfeitures.

Compensation cost for stock awards, which include restricted stock units ("RSUs"), is measured at the fair value on the grant date and recognized as expense, net of estimated forfeitures, over the related service period. The fair value of stock awards is based on the quoted price of our common stock on the grant date.

The estimated fair value of common stock option awards is calculated using the Black-Scholes option pricing model. The Black-Scholes model requires subjective assumptions regarding future stock price volatility and expected time to exercise, along with assumptions about the risk-free interest rate and expected dividends, all of which affect the estimated fair values of the Company's common stock option awards. The expected term of options granted is calculated using the simplified method, which is the weighted average vesting period and the contractual lives of the options.

This calculation is based on a method acceptable in instances where the vesting and exercise terms of options granted meet certain conditions and where limited historical exercise data is available. The expected volatility is based on the historical volatility of the common stock of comparable public companies that operate in similar industries as the Company.

The risk-free rate selected to value any particular grant is based on the U.S. Treasury rate that corresponds to the expected term of the grant effective as of the date of the grant. The expected dividend assumption is based on the Company's history and management's expectation regarding dividend payouts. Compensation expense for common stock option awards with graded vesting schedules is recognized on a straight-line basis over the requisite service period for the last separately vesting portion of the award, provided that the accumulated cost recognized as of any date at least equals the value of the vested portion of the award.

If there are any modifications or cancellations of the underlying vested or unvested stock-based awards, the Company may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense, or record additional expense for vested stock-based awards. Future stock-based compensation expense and unearned stock-based compensation may increase to the extent that the Company grants additional common stock options or other stock-based awards.

### Business Combinations

We utilize the acquisition method of accounting for business combinations and allocate the purchase price of an acquisition to the various tangible and intangible assets acquired and liabilities assumed based on their estimated fair values. We primarily establish fair value using the income approach based upon a discounted cash flow model. The income approach requires the use of many assumptions and estimates including future revenues and expenses, as well as discount factors and income tax rates. Other estimates include:

- Estimated step-ups or write-downs for fixed assets and inventory;
- Estimated fair values of intangible assets; and
- Estimated income tax assets and liabilities assumed from the target

While we use our best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business acquisition date, our estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally one year from the business acquisition date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill.

For changes in the valuation of intangible assets between preliminary and final purchase price allocation, the related amortization is adjusted in the period it occurs. Subsequent to the purchase price allocation period any adjustment to assets acquired or liabilities assumed is included in operating results in the period in which the adjustment is determined. Should we issue shares of our common stock in an acquisition, we will be required to estimate the fair value of the shares issued. See Note 3.

### Advertising Costs

Advertising costs are expensed as incurred and included in marketing and selling expense in the accompanying consolidated statements of operations. Advertising costs for the three month periods ended June 30, 2019 and 2018 were \$13,006 and \$26,754, respectively, and \$22,006 and \$44,380 for the six month periods ended June 30, 2019 and 2018.

### Research and Development Expenses

Research and development expenditures are expensed in the period incurred. Research and development expenses primarily consist of salaries, benefits and stock-based compensation, as well as consulting expenses and allocated facilities and other overhead costs. Research and development activities include the development of new technologies, features and functionality in support of the Company's products and customer needs.

### Income Taxes

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on the difference between the consolidated financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

Under ASC Topic 740, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, ASC Topic 740 provides requirements for derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company's policy is to recognize interest and/or penalties related to income tax matters in income tax expense.

The Company files income tax returns in the U.S. federal jurisdiction, California and Germany. On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act reduces the corporate tax rate to 21%, effective January 1, 2018. The Company does not foresee material changes to its gross liability of uncertain tax positions within the next twelve months.

#### Interest Expense

Interest expense consists primarily of interest associated with the Company's issued debt including the amortization of debt discounts. The Company recognizes the amortization of debt discounts and the amortization of interest costs using a straight-line method which approximates the effective interest method.

#### Net (Loss) Income Per Share

Basic net (loss) income per share is calculated by dividing net (loss) income by the weighted-average common shares outstanding during the period. Diluted net (loss) income per share is calculated by dividing the net (loss) income by the weighted-average shares and dilutive potential common shares outstanding during the period. Dilutive potential shares consist of dilutive shares issuable and the exercise or vesting of outstanding stock options and warrants, respectively, computed using the treasury stock method. During a period where a net loss is incurred, dilutive potential shares are excluded from the computation of dilutive net loss per share, as inclusion is anti-dilutive.

On February 1, 2018, in connection with the Company's initial public offering, the Company's outstanding Series A, Series B, and Series C, Preferred Stock was automatically converted to common stock, par value \$0.0001.

#### Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, *Leases* ("ASU 2016-02"). Under ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. ASU 2016-02 is effective for the Company for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early application is permitted. Lessees must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees may not apply a full retrospective transition approach. The Company is currently evaluating the impact of adopting ASU 2016-02 on its consolidated financial statements and disclosures. Based on our preliminary analysis, management expects the Company's assets and liabilities to increase by the present value of the lease payments disclosed in Note 11.

In January 2017, the FASB issued ASU No. 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business* ("ASU 2017-01"). The amendments in this update clarify the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions or disposals of assets or businesses. ASU 2017-01 will be effective for the Company for the year ending December 31, 2019 and interim reporting periods within 2020. Early adoption is permitted for transactions that have not been reported in financial statements that have been issued or made available for issuance. The Company is currently evaluating the effect of the adoption of this guidance on the Company's consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-07, *Stock-based Compensation: Improvements to Nonemployee Share-based Payment Accounting* which amends the existing accounting standards for share-based payments to nonemployees. This ASU aligns much of the guidance on measuring and classifying nonemployee awards with that of awards to employees. Under the new guidance, the measurement of nonemployee equity awards is fixed on the grant date. This ASU becomes effective for the year ending December 31, 2020 and early adoption is permitted but no earlier than an entity's adoption date of Topic 606. Entities will apply the ASU by recognizing a cumulative-effect adjustment to retained earnings as of the beginning of the annual period of adoption. We are currently evaluating the impact that ASU 2018-07 will have on our condensed consolidated financial statements.

### Recently implemented accounting pronouncements

In May 2014, the FASB issued Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers* (“ASU 2014-09”). ASU 2014-09 supersedes the revenue recognition requirements in FASB Topic 605, *Revenue Recognition*. ASU 2014-09 implements a five-step process for customer contract revenue recognition that focuses on transfer of control, as opposed to transfer of risk and rewards. This guidance provides a single, comprehensive accounting model for revenue arising from contracts with customers. This guidance supersedes most of the existing revenue recognition guidance, including industry-specific guidance. Under this model, revenue is recognized at an amount that a company expects to be entitled to upon transferring control of goods or services to a customer, as opposed to when risks and rewards transfer to a customer. The new guidance also requires additional disclosures about the nature, timing and uncertainty of revenue and cash flow arising from customer contracts, including significant judgments and changes in judgments. We adopted this standard beginning January 1, 2019 and used the modified retrospective method of adoption. Under the new guidance, based on the nature of our contracts, we continued to recognize revenue in a similar manner as with the former guidance. Additionally, we expect the unit of accounting, that is, the identification of performance obligations, will be consistent with current revenue guidance. Accordingly, the adoption of this standard did not significantly impact our revenues.

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment* (“ASU 2017-04”). ASU 2017-04 simplifies the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment testing. An entity will no longer determine goodwill impairment by calculating the implied fair value of goodwill by assigning the fair value of a reporting unit to all of its assets and liabilities as if that reporting unit had been acquired in a business combination. Instead, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value. The loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The Company adopted early ASU 2017-04 in 2018. The Company’s early adoption of this guideline did not have a material effect on the Company’s consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* (“ASU 2016-15”), which is intended to reduce the existing diversity in practice in how certain cash receipts and cash payments are classified in the statement of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted, provided that all of the amendments are adopted in the same period. The Company’s adoption of this guideline did not have a material effect on the Company’s consolidated financial statements.

### NOTE 3 – ACQUISITIONS

#### Concept Development Inc.

On August 31, 2018, the Company acquired 100% of the outstanding common stock of Concept Development Inc. (“CDI”) from CDI’s former stockholder (“CDI Stockholder”) pursuant to an Agreement and Plan of Merger and Reorganization (the “Merger Agreement”). CDI specializes in the design and manufacturing of custom high-performance computing systems for airborne in-flight entertainment systems. CDI is located in Southern California. The acquisition is expected to increase the Company’s access to the in-flight entertainment market and gain technical expertise in the design and manufacturing of airborne equipment.

The Company paid cash of \$646,759 and issued 1,266,364 shares of the Company’s common stock to the CDI Stockholder for 100% of CDI outstanding common stock. The fair value assigned to the shares of common stock was \$4,194,673, which was based upon the closing price of OSS’s stock on August 31, 2018 of \$3.63 less a discount of 8.75% for lack of marketability for a one year period.

This transaction was accounted for using the acquisition method pursuant to ASC Topic 805, *Business Combinations*. Accordingly, goodwill has been measured as the excess of the total consideration over the amounts assigned to the identifiable assets acquired and liabilities assumed.

The allocation of the total consideration to the acquired net assets as of the acquisition date for CDI is as follows:

Cash	\$	139,634
Accounts receivable		489,267
Prepaid expenses		45,683
Inventories		205,635
Property and equipment		45,026
Deposits and other		12,526
Customer lists and relationships		470,000
Trade name		90,000
Non-compete		15,000
Accounts payable		(91,997)
Accrued expenses		(99,711)
Deferred revenue		(95,610)
Deferred income taxes		(258,301)
Other accrued liabilities		(50,985)
Working capital loan		(370,096)
Total fair value excluding goodwill		546,071
Goodwill		4,295,361
Total consideration	\$	4,841,432

The preliminary determination of fair value for the identifiable net assets acquired in the acquisition was initially determined by management after consideration of the results of a third-party appraisal. At the time of acquisition, management assessed the value and recorded goodwill of \$3,100,361 and other intangible assets of \$1,770,000.

Subsequently in April 2019, and within the one year finalization period prescribed by ASC Topic 805, management finalized the valuation of assets and determined that certain assumptions in the initial financial models used for the determination of intangible asset values required modification. As a result of these modifications, identified intangible assets were reduced from \$1,770,000 to \$575,000 with the difference of \$1,195,000 being allocated to goodwill. The change in identified intangible assets is as follows:

	Preliminary Valuation	Revised Valuation	Change
Customer lists and relationships	\$ 1,470,000	\$ 470,000	\$ (1,000,000)
Trade name	100,000	90,000	(10,000)
Non-compete	200,000	15,000	(185,000)
	<u>\$ 1,770,000</u>	<u>\$ 575,000</u>	<u>\$ (1,195,000)</u>

If the revised valuation had been used since inception of the acquisition, the amortization expense would have been \$177,778 less than what has been recognized through April 2019.

Additionally, as a result of a short-fall in the actual overall financial performance of CDI as compared to plan, a recurring need for working capital, and a decrease in the Company's stock price, the Company performed an interim test of impairment of goodwill as there was indication that the carrying value of the assets may not be recoverable. To evaluate whether goodwill is impaired, the Company compares the estimated fair value of CDI to CDI's carrying value, including goodwill. The Company determined that the carrying value of CDI exceeded its estimated fair value thereby requiring the measurement of the impairment loss. After consideration of the results of an additional third-party appraisal, it was determined by management that the goodwill associated with CDI was impaired by \$1,988,701. As a result, the Company took a charge in the current period to operating expenses which is included in the accompanying consolidated statements of operations.

This business combination is considered a tax-free reorganization under Section 368(a) under the Internal Revenue Code. The Company incurred \$245,028 in accounting and legal fees related to the acquisition of CDI.

#### Bressner Technology GmbH

On October 31, 2018, the Company's wholly-owned German subsidiary, OSS GmbH, acquired 100% of the outstanding stock of Bressner Technology GmbH, a Germany limited liability company located near Munich, Germany, from its principal owners for cash consideration of €4,725,000 (US\$5,374,582) and stock consideration of 106,463 newly-issued restricted shares of the Company's common stock. The fair value assigned to the shares of common stock was \$228,779, which was based upon the closing price of OSS's stock on October 31, 2018 of \$2.47 less a discount of 13.0% for lack of marketability for a two year period.

This transaction was accounted for using the acquisition method pursuant to ASC Topic 805, *Business Combinations*. Accordingly, goodwill has been measured as the excess of the total consideration over the amounts assigned to the identifiable assets acquired and liabilities assumed.

The allocation of the total consideration to the acquired net assets as of the acquisition date for Bressner Technology GmbH is as follows:

Cash	\$	560,932
Accounts receivable		2,238,881
Inventory		3,721,685
Prepaid expenses and deposits		124,491
Fixed assets		346,637
Customer relationships		1,215,798
Trade name		329,515
Non-compete - Josef Bressner		231,797
Accounts payable and accrued expenses		(2,076,450)
Notes payable		(2,536,148)
Deferred tax liability		(43,499)
Total fair value excluding goodwill		4,113,639
Goodwill		1,489,722
Total allocated purchase price	\$	5,603,361

The determination of fair value for the identifiable net assets acquired in the acquisition was determined by management and considered the results of a third-party appraisal. Management estimates that any residual value from the intangible assets listed above will not be significant. On the acquisition date, goodwill of \$1,489,722 and other intangible assets of \$1,777,110 were recorded. The business combination is considered a tax-free reorganization under Section 368(a) under the Internal Revenue Code.

The Company incurred \$419,305 in accounting and legal fees related to the acquisition of Bressner.

Definite lived intangible assets related to acquisitions, after revaluation of CDI intangible assets, are as follows, as of June 30, 2019

	Expected Life	Remaining Months	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Customer lists and relationships	36 to 60 months	1 to 50 months	\$ 2,084,515	\$ (869,893)	\$ 1,214,622
Drawings and Technology	36 months	1 month	760,207	(749,651)	10,556
Trade name, Trademarks & other	24 to 36 months	1 to 28 months	447,274	(141,052)	306,222
Non-compete	36 months	26 to 28 months	246,797	(66,510)	180,287
			<u>\$ 3,538,793</u>	<u>\$ (1,827,106)</u>	<u>\$ 1,711,687</u>

Definite lived intangibles assets related to acquisitions are as follows, as of December 31, 2018:

	Expected Life	Remaining Months	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Customer lists and relationships	36 to 60 months	7 to 56 months	\$ 3,084,515	\$ (492,269)	\$ 2,592,246
Drawings and Technology	36 months	7 months	760,207	(622,949)	137,258
Trade name, Trademarks & other	24 to 36 months	7 to 34 months	457,274	(58,218)	399,056
Non-compete	36 months	32 to 34 months	431,797	(35,100)	396,697
			<u>\$ 4,733,793</u>	<u>\$ (1,208,536)</u>	<u>\$ 3,525,257</u>

The amortization expense of the definite lived intangible assets for the years remaining is as follows:

	2019	2020	2021	2022	2023	Total
\$	365,495	\$ 683,935	\$ 556,872	\$ 63,231	\$ 42,154	\$ 1,711,687

Amortization expense recognized during the three month periods ended June 30, 2019 and 2018 was \$269,151 and \$98,660, respectively and \$618,570 and \$197,326 for the six month periods ended June 30, 2019 and 2018.

The amount of revenue and net loss of CDI included in the Company's consolidated statements of operations for the three month periods ended June 30, 2019 was \$894,562 and \$2,109,285, respectively and \$1,194,016 and \$2,472,814 for the six month periods ended June 30, 2019. The amount of revenue and net loss of Bressner included in the Company's consolidated statements of operations for the three month periods ended June 30, 2019 was \$4,018,495 and \$31,579, respectively, and \$8,554,099 and \$180,738 for the six month periods ended June 30, 2019. The following unaudited consolidated pro forma information presents the results of operations for the three and six month periods ended June 30, 2019 and 2018 as if these two acquisitions occurred on January 1, 2018.

	For The Three Months Ended June 30,		For The Six Months Ended June 30,	
	2019	2018	2019	2018
Revenue	\$ 14,886,236	\$ 11,701,055	\$ 24,944,135	\$ 22,670,523
Net loss	\$ (1,090,176)	\$ (962,168)	\$ (2,034,905)	\$ (1,864,160)
Acquisition-related pro forma net loss per share attributable to common stockholders				
Basic	\$ (0.08)	\$ (0.08)	\$ (0.14)	\$ (0.16)
Diluted	\$ (0.08)	\$ (0.08)	\$ (0.14)	\$ (0.16)

**NOTE 4 – ACCOUNTS RECEIVABLE**

Accounts receivable, net consists of the following:

	June 30, 2019	December 31, 2018
Accounts receivable	\$ 8,274,313	\$ 10,488,396
Unbilled receivables	81,826	65,157
	<u>8,356,139</u>	<u>10,553,553</u>
Less: allowance for doubtful accounts	(14,727)	(13,403)
	<u>\$ 8,341,412</u>	<u>\$ 10,540,150</u>

Unbilled receivables include amounts associated with percentage-of-completion accounting, which includes cost and gross profit earned in excess of billing, not currently billable due to contractual provisions. The provision for bad debt expense related to accounts receivable was \$1,446 and \$3,304 for the three month periods ended June 30, 2019 and 2018, respectively and \$1,358 and \$94,431 for the six month periods ended June 30, 2019 and 2018, respectively.

**NOTE 5 – INVENTORIES**

Inventories, net consist of the following:

	June 30, 2019	December 31, 2018
Raw materials	\$ 3,006,116	\$ 2,248,520
Sub-assemblies	1,356,342	1,198,071
Work-in-process	524,211	311,072
Finished goods	4,388,052	3,466,419
	<u>9,274,721</u>	<u>7,224,082</u>
Less: reserves for obsolete and slow-moving inventories	(415,440)	(400,152)
	<u>\$ 8,859,281</u>	<u>\$ 6,823,930</u>

**NOTE 6 – PROPERTY AND EQUIPMENT**

Property and equipment, net consists of the following:

	June 30, 2019	December 31, 2018
Computers and computer equipment	\$ 639,858	\$ 609,921
Furniture and office equipment	329,519	211,759
Manufacturing equipment and engineering tools	2,439,519	2,211,080
Leasehold improvements	812,167	163,373
	<u>4,221,063</u>	<u>3,196,133</u>
Less: accumulated depreciation and amortization	(2,127,611)	(1,880,167)
	<u>2,093,452</u>	<u>1,315,966</u>
Construction in progress - facilities	4,432	197,619
Software implementation in progress - ERP	742,355	245,501
	<u>\$ 2,840,239</u>	<u>\$ 1,759,086</u>

During the three month periods ended June 30, 2019 and 2018, the Company incurred \$163,301 and \$176,072 respectively, and \$268,412 and \$331,168 for the six month periods ended June 30, 2019 and 2018, respectively of depreciation and amortization expense related to property and equipment.

**NOTE 7 – ACCRUED EXPENSES AND OTHER LIABILITIES**

Accrued expenses and other liabilities consist of the following:

	June 30, 2019	December 31, 2018
Accrued compensation and related liabilities	\$ 975,858	\$ 1,183,653
Deferred revenue and customer deposits	3,661,717	1,135,470
Warranty reserve	418,862	416,313
Other accrued expenses	960,814	1,195,282
	<u>\$ 6,017,251</u>	<u>\$ 3,930,718</u>

**NOTE 8 – DEBT**Bank Lines of Credit

Bressner Technology GmbH has four revolving lines of credit with German institutions totaling €3,800,000 (US\$4,320,562). Borrowing under the lines of credit bear interest at variable rates of Euribor plus a stated rate. Current rates are between 3.75% and 7.99%. The lines of credit are guaranteed by the managing director. Total outstanding balance as of June 30, 2019 was €934,354 (US\$1,062,352).

Notes Payable

In connection with July 2016 Note, the Company issued to the noteholder warrants to purchase shares of the Company's common stock equal to 20% of the original principal at a price per share equal to \$1.78 per share. Accordingly, the Company issued to the noteholder warrants to purchase 28,090 shares of the Company's common stock at an exercise price of \$1.78 per share in July 2016. The relative fair value of the warrants was \$24,830. The relative fair value of warrants was estimated using Black-Scholes with the following weighted-average assumptions: fair value of the Company's common stock at issuance of \$1.78 per share; seven year contractual term; 54% volatility; 0% dividend rate; and a risk-free interest rate of 1.42%.

In April 2019, the Company borrowed \$350,000 from three individuals for a two year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payments of \$16,100 per month. These loans are secured by the assets of the Company. In connection with these loans, the Company issued to the noteholders warrants to purchase shares of the Company's common stock equal to 10% of the original principle at a price per share equal to \$2.15 per share. Accordingly, the Company issued to the noteholders warrants to purchase 16,276 shares of the Company's common stock at an exercise price of \$2.15 per share. The relative fair value of each warrant was \$0.89831. The relative fair value of warrants was estimated using Black-Scholes with the following weighted-average assumptions: fair value of the Company's common stock at issuance of \$2.15 per share; five year contractual term; 44.60% volatility; 0.0% dividend rate; and a risk-free interest rate of 2.307%. The total relative fair value of the warrants issued is \$14,037.

Bressner Technology GmbH has six term loans outstanding with a total balance outstanding of €1,587,734 (US\$1,805,239) as follows:

Bressner entered into an unsecured note payable for working capital in August 2015, in the amount of €250,000 (US\$284,248) which bears interest at 2.125% which matures on August 31, 2019. Quarterly principal payments of €15,703 (US\$17,618) are due at the beginning of each calendar quarter with remaining balance due at maturity. The balance outstanding as of June 30, 2019 is €17,562 (US\$19,968).

Bressner entered into a note payable in August 2016, in the amount of €250,000 (US\$284,248) which bears interest at 2.125% which matures on September 30, 2020. The loan is guaranteed by the managing director of Bressner. Quarterly principal payments of €15,600 (US\$17,504) are due at the end of each calendar quarter with remaining balance due at maturity. The balance outstanding as of June 30, 2019 is €62,800 (US\$71,403).

Bressner entered into a note payable in September 2017, in the amount of €400,000 (US\$454,796) which bears interest at 2.125% which matures on April 30, 2020. The loan was guaranteed by the managing director of Bressner. Quarterly principal payments of €25,000 (US\$28,051) are due in January, April, July and November with remaining balance of €175,000 (US\$196,362) due at maturity. The balance outstanding as of June 30, 2019 is €250,000 (US\$284,248).

Bressner entered into a note payable in April 2019, in the amount of €500,000 (US\$568,495) which bears interest at 2.25% which matures on March 30, 2021 with monthly payments of principal and interest of €21,324 (US\$24,244). The balance outstanding as of June 30, 2019 is €457,372 (US\$520,027).

Bressner entered into a note payable in June 2019, in the amount of €500,000 (US\$568,495) which bears interest at 1.7075% which matures on June 25, 2020 with a balloon payment of principal and interest of €508,679 (US\$578,362).

Bressner entered into a note payable in June 2019, in the amount of €300,000 (US\$341,096) which bears interest at 1.65% which matures on March 24, 2020 with a balloon payment of principal and interest of €303,716 (US\$345,322).

#### Related-Party Notes Payable

In April 2019, the Company borrowed \$1,150,000 from three individuals who serve on the Company's board of directors for a two year period at an interest rate of 9.5% which requires the Company to make monthly principal and interest payments of \$52,900 per month. These loans are secured by the assets of the Company. In connection with these loans, the Company issued to the noteholders warrants to purchase shares of the Company's common stock equal to 10% of the original principal at a price per share equal to \$2.15 per share. Accordingly, the Company issued to the noteholders warrants to purchase 53,490 shares of the Company's common stock at an exercise price of \$2.15 per share. The relative fair value of each warrant was \$0.89831. The relative fair value of warrants was estimated using Black-Scholes with the following weighted-average assumptions: fair value of the Company's common stock at issuance of \$2.15 per share; five year contractual term; 42.60% volatility; 0.0% dividend rate; and a risk-free interest rate of 2.3067%. The relative fair value of warrants issued is \$46,121.

#### Debt Discount

The relative fair value of warrants were recorded as debt discount, decreasing notes payable and related-party notes payable and increasing additional paid-in-capital on the accompanying consolidated balance sheets. The debt discounts are being amortized to interest expense over the term of the corresponding notes payable using the straight-line method which approximates the effective interest method.

For the three and six month periods ended June 30, 2019, total debt discount amortization was \$6,266 and \$6,266, respectively, and is included in interest expense in the accompanying consolidated statements of operations.

Total future payments under notes payable and related-party notes payable as of June 30, 2019 are as follows:

<u>Period Ending June 30,</u>	<u>Related Parties</u>	<u>Third Parties</u>	<u>Foreign</u>	<u>Total</u>	<u>Discount</u>
2019	\$ 557,145	\$ 169,541	\$ 1,566,847	\$ 2,293,533	\$ 30,080
2020	505,851	154,230	238,392	898,473	23,812
Total minimum payments	1,062,996	323,771	1,805,239	3,192,006	53,892
Current portion of notes payable	(557,145)	(169,541)	(1,566,847)	(2,293,533)	(30,080)
Notes payable, net of current portion	<u>\$ 505,851</u>	<u>\$ 154,230</u>	<u>\$ 238,392</u>	<u>\$ 898,473</u>	<u>\$ 23,812</u>

#### NOTE 9 – STOCKHOLDERS' EQUITY

The Company's amended and restated certificate of incorporation filed on December 14, 2017, authorizes the Company to issue 10,000,000 shares of preferred stock and 50,000,000 shares of common stock. On February 1, 2018, in connection with the Company's initial public offering, each share of the Company's outstanding Series A, Series B, and Series C, Preferred Stock was automatically converted into a share of the Company's common stock, par value \$0.0001 on a one-for-one basis.

### Follow-on Public Offering

On May 15, 2019, the Company filed an S-3 prospectus with the Securities and Exchange Commission which became effective on June 19, 2019, and allows the Company to offer up to \$100,000,000 aggregate dollar amount of shares of its common stock, preferred stock, debt securities, warrants to purchase its common stock, preferred stock or debt securities, subscription rights to purchase its common stock, preferred stock or debt securities and/or units consisting of some or all of these securities, in any combination, together or separately, in one or more offerings, in amounts, at prices and on the terms that the Company will determine at the time of the offering and which will be set forth in a prospectus supplement and any related free writing prospectus.

On June 26, 2019, the Company filed a prospectus supplement relating to its common stock, par value \$0.0001 per share, whereby under the prospectus supplement the Company may offer and sell common stock having an aggregate offering price of up to \$10,000,000 through Noble Capital Markets, Inc., (“Noble”) acting as the Company’s agent. As such, the Company entered into an Equity Distribution Agreement with Noble dated as of June 26, 2019. As of July 31, 2019, the Company has sold 1,019,561 shares of common stock through this offering for total gross proceeds of \$1,773,332, which resulted in net proceeds to us of \$1,746,046, after deducting compensation payable to Noble of \$27,286.

### Exercise of Stock Options and Warrants

During the six month periods ended June 30, 2019, the Company issued 281,319 shares of common stock for proceeds of \$21,149 in cash related to the exercise of stock options and warrants. Of the total shares issued, 234,619 shares of common stock were issued as a cashless exercise of stock options.

### Stock Options

A summary of stock option activity under each of the Company’s stock option plans during the six month period ended June 30, 2019 is as follows:

	<b>Stock Options Outstanding</b>			
	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Life (in years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at January 1, 2019	1,968,747	\$ 1.14	4.56	\$ 1,469,525
Granted	56,000	\$ 2.43	-	-
Forfeited / Cancelled	(12,000)	\$ 3.02	-	-
Exercised	(446,669)	\$ 0.48	-	-
Outstanding at June 30, 2019	<u>1,566,078</u>	<u>\$ 1.37</u>	<u>5.80</u>	<u>\$ 918,390</u>
Exercisable at June 30, 2019	<u>1,278,291</u>	<u>\$ 1.04</u>	<u>5.14</u>	<u>\$ 918,390</u>
Vested and expected to vest at June 30, 2019	<u>1,559,217</u>	<u>\$ 1.35</u>	<u>5.78</u>	<u>\$ 918,390</u>

The following table presents details of the assumptions used to calculate the weighted-average grant date fair value of common stock options granted by the Company:

	<b>For The Six Months Ended June 30,</b>	
	<b>2019</b>	<b>2018</b>
Expected term (in years)	4.65 - 5.87	-
Expected volatility	43.7 - 44.4%	-
Risk-free interest rate	2.49 - 2.55%	-
Weighted average grant date fair value per share	\$ 1.07	-
Grant date fair value of options vested	<u>\$ 574,524</u>	<u>\$ 1,376,865</u>
Intrinsic value of options exercised	<u>\$ 551,134</u>	<u>\$ 20,235</u>

As of June 30, 2019, the amount of unearned stock-based compensation estimated to be expensed from 2019 through 2022 related to unvested common stock options is \$263,505, net of estimated forfeitures. The weighted-average period over which the unearned stock-based compensation is expected to be recognized is 1.88 years.

If there are any modifications or cancellations of the underlying unvested awards, the Company may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense or calculate and record additional expense. Future stock-based compensation expense and unearned stock-based compensation will increase to the extent that the Company grants additional common stock options or other stock-based awards.

#### Restricted Stock Units

Restricted stock units may be granted at the discretion of the compensation committee of the Board of Directors under the 2017 Plan in connection with the hiring and retention of personnel and are subject to certain conditions. Restricted stock units generally vest quarterly or semi-annually over a period of one to three years and are typically forfeited if employment is terminated before the restricted stock unit vest. The compensation expense related to the restricted stock units is calculated as the fair value of the common stock on the grant date and is amortized to expense over the vesting period and is adjusted for estimated forfeitures.

The Company's restricted stock unit activity for the six month period ended June 30, 2019 is as follows:

	<b>Restricted Stock Units</b>	
	<b>Number of Shares</b>	<b>Weighted Average Grant Date Fair Value</b>
Unvested at January 1, 2019	173,335	\$ 4.13
Granted	160,000	\$ 2.43
Vested	(67,500 )	\$ 4.15
Cancelled	-	\$ -
Unvested at June 30, 2019	<u>265,835</u>	<u>\$ 3.10</u>

As of June 30, 2019, there was \$652,907 of unrecognized compensation cost related to unvested restricted stock units which is expected to be recognized over a weighted average period of 1.3 years.

Stock-based compensation expense for the three and six month periods ended June 30, 2019 and 2018 was comprised of the following:

	<b>For The Three Months Ended June 30,</b>		<b>For The Six Months Ended June 30,</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Stock-based compensation classified as:				
General and administrative	\$ 119,231	\$ 104,621	\$ 244,438	\$ 126,441
Production	12,146	3,273	27,044	6,463
Marketing and selling	15,067	7,866	29,460	10,815
Research and development	11,363	9,056	24,341	16,414
	<u>\$ 157,807</u>	<u>\$ 124,816</u>	<u>\$ 325,283</u>	<u>\$ 160,133</u>

## Warrants

The following table summarizes the Company's warrant activity during the six month period ended June 30, 2019:

	Number of Warrants	Weighted Average Exercise Price
Warrants outstanding – January 1, 2019	578,996	\$ 4.32
Warrants granted	69,766	\$ 2.15
Warrants exercised	(17,815)	\$ 1.40
Warrants outstanding – June 30, 2019	630,947	\$ 4.16

## **NOTE 10 – EMPLOYEE BENEFIT PLAN**

The Company has a 401(k) retirement plan. Under the terms of the plan, eligible employees may defer up to 20% of their pre-tax earnings, subject to the Internal Revenue Service annual contribution limit. Additionally, the Plan allows for discretionary matching contributions by the Company. In the six month periods ended June 30, 2019 and 2018, the matching contributions were 100% of the employee's contribution up to a maximum of 5% of the employee's annual compensation. During the three month periods ended June 30, 2019 and 2018, the Company contributed \$81,356 and \$78,071, respectively, and \$172,728 and \$152,718 for the six month periods ended June 30, 2019 and 2018, respectively, to the 401(k) Plan.

## **NOTE 11 – COMMITMENTS AND CONTINGENCIES**

### Legal

From time to time the Company is subject to various legal claims and proceedings arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of any such matters as of June 30, 2019 and December 31, 2018, will not have a materially adverse effect on the consolidated financial position or results of operations of the Company.

### Guarantees and Indemnities

The Company has made certain indemnities, under which it may be required to make payments to an indemnified party, in relation to certain transactions. The Company indemnifies its directors, officers, employees and agents to the maximum extent permitted under the laws of the State of Delaware. In connection with its facility lease, the Company has indemnified its lessor for certain claims arising from the use of the facilities. Also, in connection with its Credit Agreement (Note 8), the Company has agreed to indemnify its lender and others related to the use of the proceeds and other matters. The duration of the indemnities varies, and in many cases is indefinite. These indemnities do not provide for any limitation of the maximum potential future payments the Company could be obligated to make. Historically, the Company has not been obligated to make any payments for these obligations and no liabilities have been recorded for these indemnities in the accompanying consolidated balance sheets.

### Leases

The Company leases its offices, manufacturing, and warehouse facility in San Diego County under a non-cancelable operating lease. Our corporate headquarters are in a leased space comprising approximately 24,032 square feet in Escondido, California under a lease that was renewed in August 2018 and expires in August 2024. We also lease a 3,208 square foot facility in Salt Lake City, Utah that houses our Ion software development team. CDI is the lessee of approximately 12,000 square feet located in Irvine, California with the lease expiring in June 2021. Bressner Technology GmbH, which was acquired in October 2018, leases space comprising 8,073 square feet which lease expires in December 2019.

For the three month periods ended June 30, 2019 and 2018, rent expense was \$167,870 and \$152,534, respectively. For the six month periods ended June 30, 2019 and 2018, rent expense was \$339,015 and \$296,462, respectively.

**NOTE 12 – RELATED PARTY TRANSACTIONS**

The Company has engaged an advertising firm whose president is a member of the Board of Directors of the Company. Amounts paid to this company are included in marketing and selling expense in the accompanying consolidated statements of operations and for the three month periods ended June 30, 2019 and 2018, totaled \$13,006 and \$12,000, respectively and for the six month periods ended June 30, 2019 and 2018, totaled \$22,006 and \$ 16,000, respectively.

The Company has appointed certain stockholders to the Board of Directors. Director fees paid by the Company, including stock-based compensation, for the three month periods ended June 30, 2019 and 2018 totaled \$18,613 and \$64,018, respectively, and for the six month periods ended June 30, 2019 and 2018 totaled \$101,449 and \$100,468, respectively which is included in general and administrative expenses in the accompanying consolidated statements of operations.

The Company has engaged a related-party law firm (a principal of that firm owns shares in the Company) to provide legal services. Legal fees paid to this firm are included in general and administrative expenses in the accompanying consolidated statements of operations for the three month periods ended June 30, 2019 and 2018 totaled \$6,000 and \$32,093, respectively and \$18,000 and \$42,090 for the six month periods June 30, 2019 and 2018, respectively.

The Company has engaged an IT network support firm whose owner is an employee of the Company. Fees paid to this firm are included in general and administrative expense in the accompanying consolidated statements of operations for the three month periods ended June 30, 2019 and 2018 totaled \$516 and \$3,627 and \$1,176 and \$6,491 for the six month periods ended June 30, 2019 and 2018, respectively.

Interest expense on all related-party notes payable for the three and six month periods ended June 30, 2019 and 2018 totaled \$23,223 and \$23,223 and \$0 and \$16,599, respectively.

Effective August 1, 2016, the Company entered into a management services agreement with a company owned by the former Chief Executive Officer of Magma. The agreement calls for payments of \$180,000 per year for the first two years paid in monthly installments. In year three, the amount is reduced to \$37,500 for the year paid in monthly installments. Additionally, the Company granted 30,000 options in conjunction with execution of this agreement. Payments for the three month periods ended June 30, 2019 and 2018 were \$9,375 and \$45,000, respectively and \$18,750 and \$90,000 for the six month periods ended June 30, 2019 and 2018, respectively.

**NOTE 13 – NET LOSS PER SHARE**

Basic and diluted net loss per share was calculated as follows for the three and six month periods ended June 30, 2019 and 2018:

	<u>For The Three Months Ended June 30,</u>		<u>For The Six Months Ended June 30,</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Basic and diluted net loss per share attributable to common stockholders:				
Numerator:				
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)
Denominator:				
Weighted average common shares outstanding - basic	14,442,291	12,773,419	14,341,560	11,464,246
Effect of dilutive securities	-	-	-	-
Weighted average common shares outstanding - diluted	<u>14,442,291</u>	<u>12,773,419</u>	<u>14,341,560</u>	<u>11,464,246</u>
Net loss per common share attributable to common stockholders:				
Basic	\$ (0.11)	\$ (0.12)	\$ (0.18)	\$ (0.20)
Diluted	<u>\$ (0.11)</u>	<u>\$ (0.12)</u>	<u>\$ (0.18)</u>	<u>\$ (0.20)</u>

**NOTE 14 – FAIR VALUE MEASUREMENTS**

The Company uses a three-tier fair value hierarchy to classify and disclose all assets and liabilities measured at fair value on a recurring basis, as well as assets and liabilities measured at fair value on a non-recurring basis, in periods subsequent to their initial measurement. These tiers include:

- Level 1, defined as quoted market prices in active markets for identical assets or liabilities;
- Level 2, defined as inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, model-based valuation techniques for which all significant assumptions are observable in the market, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3, defined as unobservable inputs that are not corroborated by market data.

The carrying value of financial instruments including cash and cash equivalents accounts receivable and accounts payable and accrued expenses, lines of credit, and other liabilities approximate fair value due to the short-term nature of these instruments. Assets and liabilities assumed in the acquisition of the Ion software, Concept Development Inc., and Bressner Technology GmbH were recorded at fair value based upon the Company's market assumptions which approximated carrying value (except for acquired intangible assets – Note 2) due to the short-term nature of the instruments. The carrying amounts of Bressner's existing lines of credit and notes payable approximate their fair values at the stated interest rates and are reflective of the prevailing market rates.

**NOTE 15 – SEGMENT AND GEOGRAPHIC INFORMATION**

The Company operates in three reportable segments: the design and manufacture of high-performance customized computers and flash arrays, in-flight entertainment & connectivity and value-added reseller with minimal customization. The Company evaluates financial performance on a company-wide basis.

Segment detail for the three and six month periods ended June 30, 2019 and 2018 is as follows:

	For The Three Month Periods ended June 30, 2019				For The Three Month Periods ended June 30, 2018			
	OSS	CDI	Bressner	Total	OSS	CDI	Bressner	Total
Revenues	\$ 10,007,804	\$ 894,562	\$ 3,983,870	\$ 14,886,236	\$ 5,892,666	\$ -	\$ -	\$ 5,892,666
Cost of revenues	(5,712,191)	(717,717)	(3,043,170)	(9,473,078)	(4,252,484)	-	-	(4,252,484)
Gross profit	4,295,613	176,845	940,700	5,413,158	1,640,182	-	-	1,640,182
Gross profit %	42.92 %	19.77 %	23.61 %	36.36 %	27.83 %	-	-	27.83 %
Total operating expenses	3,240,943	2,222,460	930,235	6,393,638	2,758,801	-	-	2,758,801
Income (loss) from operations	\$ 1,054,670	\$ (2,045,615)	\$ 10,465	\$ (980,480)	\$ (1,118,619)	\$ -	\$ -	\$ (1,118,619)
	For The Six Month Periods ended June 30, 2019				For The Six Month Periods ended June 30, 2018			
	OSS	CDI	Bressner	Total	OSS	CDI	Bressner	Total
Revenues	\$ 15,237,890	\$ 1,194,016	\$ 8,512,229	\$ 24,944,135	\$ 13,012,378	\$ -	\$ -	\$ 13,012,378
Cost of revenues	(9,441,095)	(1,063,444)	(6,614,815)	(17,119,354)	(9,159,330)	-	-	(9,159,330)
Gross profit	5,796,795	130,572	1,897,414	7,824,781	3,853,048	-	-	3,853,048
Gross profit %	38.04 %	10.94 %	22.29 %	31.37 %	29.61 %	-	-	29.61 %
Total operating expenses	6,380,909	2,503,676	1,952,885	10,837,470	5,673,495	-	-	5,673,495
Loss from operations	\$ (584,114)	\$ (2,373,104)	\$ (55,471)	\$ (3,012,689)	\$ (1,820,447)	\$ -	\$ -	\$ (1,820,447)

Revenue from customers with non-U.S. billing addresses represented approximately 58% and 55% of the Company's revenue during the three month periods ended June 30, 2019 and 2018, respectively and 63% and 50% for the six month periods ended June 30, 2019 and 2018, respectively

As of June 30, 2019, substantially all the Company's long-lived assets were located in the United States of America with the exception of assets of \$309,348 located in Germany.

**NOTE 16 – SUBSEQUENT EVENTS**

Resulting from the follow-on public offering, as of July 31, 2019, the Company has sold 1,019,561 shares of common stock through this offering for total gross proceeds of \$1,773,332, which resulted in net proceeds to us of \$1,746,046, after deducting compensation payable to Noble of \$27,286.

The Company has evaluated subsequent events after the consolidated balance sheet date of June 30, 2019 through the date of filing. Based upon the Company's evaluation, management has determined that, other than as disclosed in the accompanying notes, no subsequent events have occurred that would require recognition in the accompanying consolidated financial statements or disclosure in the notes thereto.

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

*You should read the following discussion and analysis of our financial condition and operating results together with our financial statements and related notes included elsewhere in this Quarterly Report. This discussion and analysis contains forward-looking statements based upon current beliefs, plans and expectations that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under “Risk Factors” or in other parts of this Quarterly Report.*

### Overview

OSS designs, manufactures and markets custom high speed computing systems for high performance computing (HPC) applications. These applications require ultra-fast processing power and the ability to quickly access and store ever-growing data sets. Systems are built using the latest GPU (graphical processing unit) and solid-state flash (memory) technologies. We are a niche provider of HPC custom servers, compute accelerators, and flash storage arrays. We deliver this technology to customers through sale of equipment and software to customers. Concept Development Inc., (CDI) which was acquired on August 31, 2018, specializes in the design and manufacture of specialized high-performance in-flight entertainment systems for commercial aircraft. CDI’s capabilities include electrical, mechanical and software design as well as extensive experience in test and certifications required for airborne systems. Bressner Technology GmbH, (Bressner) which was acquired on October 31, 2018, provides standard and customized servers, panel PCs, and PCIe expansion systems. Bressner provides manufacturing, test, sales and marketing services for customers throughout Europe.

### Business Developments

On August 31, 2018, the Company acquired Concept Development Inc. (CDI) located in Irvine, California for cash of \$646,759, and common stock of \$4,194,673. CDI specializes in the design and manufacture of custom high-performance computing systems for airborne in-flight entertainment systems.

On October 31, 2018, the Company’s wholly-owned German subsidiary, OSS GmbH, acquired 100% of the outstanding stock of Bressner Technology GmbH, a Germany limited liability company located near Munich, Germany, from its principal owners for cash consideration of €4,725,000 (US\$5,374,582) and stock consideration of 106,463 newly-issued restricted shares of the Company’s common stock with an estimated fair value of \$228,779.

On December 31, 2018, as a result of changes in the competitive landscape and downward pressure on pricing from large competitors, the members to the joint venture agreement agreed to begin the dissolution of SkyScale.

During the quarter ended June 30, 2019, as a result of a short-fall in the actual overall financial performance of CDI as compared to plan, a recurring need for working capital, and a decrease in the Company’s stock price, the Company performed an interim test of impairment of goodwill as there was indication that the carrying value of the assets may not be recoverable. As a result it was determined by management that the goodwill associated with CDI was impaired by \$1,988,701 and as a result took a charge to operating expenses.

### Our Business Model

OSS designs, manufactures and sells specialized high performance computing (HPC) systems to customers world-wide. We differentiate ourselves from other suppliers of HPC solutions by utilizing our expertise in custom systems design and PCIe expansion to build systems with a greater quantity of PCIe add-in slots, GPU-based compute cards and/or flash cards. Our systems offer industry leading capabilities that occupy less physical space and power consumption.

Concept Development, LLC focuses on engineering innovative products and solutions that enhances success for our clients in their design, manufacturing and life support cycle, with in-flight entertainment and connectivity of their processes enabling efficiencies and cost savings.

Bressner Technology GmbH is a leading provider of industrial IT solutions with long standing international contact to assist in leveraging markets around the world to our customers benefit and give them early access to innovative new products. By continuing to forge strategic partnerships, we have significantly expanded our range of services. With this, we offer consistent product portfolio at all integration levels, superior product quality, efficient logistics and excellent support.

## **Components of Results of Operations**

### *Revenue*

On January 1, 2019, the Company adopted the new accounting standard update ASC 606, Revenue from Contracts with Customers, which superseded nearly all existing revenue recognition guidance under GAAP, to all contracts using the modified retrospective method. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The adoption of ASC 606 did not have a material impact on our results of operations for the current periods.

The Company's contracts are executed through a combination of written agreements along with purchase orders with all customers including certain general terms and conditions. Generally, purchase orders entail products, quantities and prices, which define the performance obligations of each party and are approved and accepted by the Company. The Company's performance obligations are satisfied over time as work is performed or at a point in time. The majority of the Company's revenue is recognized at a point in time when products ship and control is transferred to the customer.

Customer agreements include one vendor managed inventory program. Such arrangement must be requested by the customer and the customer has explained a substantial business purpose for the arrangement. Management also considers whether the customer's custodial risks are insured and whether modifications to the Company's normal billing and credit terms were required.

Revenues on certain fixed-price contracts where we provide engineering services, prototypes and completed products are recognized over the contract term based on the percentage of completion or based upon milestones delivered that are provided during the period and compared to the total estimated development and milestone goals to be provided over the entire contract. Performance will often extend over long periods of time, and our right to receive future payment depends on our future performance in accordance with the agreement.

The percentage-of-completion methodology involves recognizing probable and reasonably estimable revenue using the percentage of services completed, on a current cumulative cost to estimate total cost basis, using a reasonably consistent profit margin over the period. Due to the long-term nature of these projects, developing the estimates of costs often requires significant judgment. .

Related billings that are in excess of revenue earned are deferred and recorded as a liability on the balance sheet until the related services are provided. The Company recognizes revenues for non-refundable, upfront implementation fees on a straight-line basis over the period beginning with initiation of ongoing services through the end of the contract term.

### *Cost of revenue*

Cost of revenue primarily consists of costs of materials, costs paid to third-party contract manufacturers (which may include the costs of components), and personnel costs associated with manufacturing and support operations. Personnel costs consist of wages, bonuses, benefits, stock-based compensation expenses. Cost of revenue also includes freight, allocated overhead costs and inventory write-offs and changes to our inventory and warranty reserves. Allocated overhead costs consist of certain facilities and utility costs. We expect cost of revenue to increase in absolute dollars, as product revenue increases.

### *Operating expenses*

Our operating expenses consist of general and administrative, sales and marketing and research and development expenses. Salaries and personnel-related costs, benefits, and stock-based compensation expense, are the most significant components of each category of operating expenses. Operating expenses also include allocated overhead costs for facilities and utility costs.

*General and Administrative* - General and administrative expense consists primarily of employee compensation and related expenses for administrative functions including finance, legal, human resources and fees for third-party professional services, as well as allocated overhead. For 2018, general and administrative expenses include the costs related to the operations of SkyScale, LLC. We expect our general and administrative expense to increase in absolute dollars as we continue to invest in growing the business.

*Sales and Marketing* - Sales and marketing expense consists primarily of employee compensation and related expenses, sales commissions, marketing programs, travel and entertainment expenses as well as allocated overhead. Marketing programs consist of advertising, tradeshows, events, corporate communications and brand-building activities. We expect sales and marketing expenses to increase in absolute dollars as we expand our sales force, increase marketing resources, and further develop sales channels.

*Research and Development* - Research and development expense consists primarily of employee compensation and related expenses, prototype expenses, depreciation associated with assets acquired for research and development, third-party engineering and contractor support costs, as well as allocated overhead. We expect our research and development expenses to increase in absolute dollars as we continue to invest in new and existing products.

### *Other Income (Expense), net*

Other income consists of income received for activities outside of our core business. Other expense includes expenses for activities outside of our core business. These expenses consist primarily of loan fee amortization and interest expense.

### *Provision for Income Taxes*

Provision for income taxes consists of estimated income taxes due to the United States and German governments and to the state tax authorities in jurisdictions in which we conduct business, as well as the change in our deferred income tax assets and liabilities.

## **Results of Operations**

Results of operations for the three and six month periods ended June 30, 2019 and 2018 include the following businesses from the date of their acquisition: Magma, SkyScale, which began operations in April 2017 and ceased operations on December 31, 2018, the purchase of the Ion business from Western Digital on July 1, 2017, Concept Development Inc., which was acquired on August 31, 2018, and Bressner Technology GmbH, which was acquired on October 31, 2018.

Accordingly, the periods presented below are not directly comparable. After the completion of four quarters, these businesses for both revenue and expense reporting will be treated as organic operating activity for current and comparable historical periods.

The following tables set forth our results of operations for the three and six month periods ended June 30, 2019 and 2018 respectively, presented in dollars and as a percentage of net revenue.

	For The Three Month Periods ended June 30,		For The Six Month Periods ended June 30,	
	2019	2018	2019	2018
Net revenue	\$ 14,886,236	\$ 5,892,666	\$ 24,944,135	\$ 13,012,378
Cost of revenue	9,473,078	4,252,484	17,119,354	9,159,330
Gross margin	5,413,158	1,640,182	7,824,781	3,853,048
Operating expenses:				
General and administrative	3,931,478	1,097,552	5,975,413	2,170,600
Marketing and selling	1,237,003	702,474	2,374,936	1,571,489
Research and development	1,225,157	958,775	2,487,121	1,931,406
Total operating expenses	6,393,638	2,758,801	10,837,470	5,673,495
Loss from operations	(980,480)	(1,118,619)	(3,012,689)	(1,820,447)
Other income (expense):				
Interest expense	(53,013)		(59,281)	(55,661)
Other, net	(3,068)	54,430	(11,232)	122,039
Total other (expense) income, net	(56,081)	54,430	(70,513)	66,378
Loss before income taxes	(1,036,561)	(1,064,189)	(3,083,202)	(1,754,069)
Provision (benefit) for income taxes	558,072	555,629	(543,839)	772,752
Net loss	\$ (1,594,633)	\$ (1,619,818)	\$ (2,539,363)	\$ (2,526,821)
Net loss attributable to noncontrolling interest	\$ -	\$ (116,996)	\$ -	\$ (229,581)
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)

	For The Three Month Periods ended June 30,		For The Six Month Periods ended June 30,	
	2019	2018	2019	2018
Net revenue	100.0%	100.0%	100.0%	100.0%
Cost of revenue	63.6%	72.2%	68.6%	70.4%
Gross margin	36.4%	27.8%	31.4%	29.6%
Operating expenses:				
General and administrative	26.4%	18.6%	24.0%	16.7%
Marketing and selling	8.3%	11.9%	9.5%	12.1%
Research and development	8.2%	16.3%	10.0%	14.8%
Total operating expenses	42.9%	46.8%	43.4%	43.6%
Loss from operations	-6.6%	-19.0%	-12.1%	-14.0%
Other income (expense):				
Interest expense	-0.4%	0.0%	-0.2%	-0.4%
Other, net	0.0%	0.9%	0.0%	0.9%
Total other (expense) income, net	-0.4%	0.9%	-0.3%	0.5%
Loss before income taxes	-7.0%	-18.1%	-12.4%	-13.5%
Provision (benefit) for income taxes	3.7%	9.4%	-2.2%	5.9%
Net loss	-10.7%	-27.5%	-10.2%	-19.4%
Net loss attributable to noncontrolling interest	0.0%	-2.0%	0.0%	-1.8%
Net loss attributable to common stockholders	-10.7%	-25.5%	-10.2%	-17.7%

## Non-GAAP Financial Measures

### Adjusted EBITDA

We believe that the use of adjusted earnings before interest, taxes, depreciation and amortization, or adjusted EBITDA, is helpful for an investor to assess the performance of the Company. The Company defines adjusted EBITDA as income (loss) attributable to common stockholders before interest, taxes, depreciation, amortization, acquisition expenses, impairment of long-lived assets, financing costs, fair value adjustments from purchase accounting, stock-based compensation expense and expenses related to discontinued operations.

Adjusted EBITDA is not a measurement of financial performance under generally accepted accounting principles in the United States, or GAAP. Because of varying available valuation methodologies, subjective assumptions and the variety of equity instruments that can impact a company's non-cash operating expenses, we believe that providing a non-GAAP financial measure that excludes non-cash and non-recurring expenses allows for meaningful comparisons between our core business operating results and those of other companies, as well as providing us with an important tool for financial and operational decision making and for evaluating our own core business operating results over different periods of time.

Our adjusted EBITDA measure may not provide information that is directly comparable to that provided by other companies in our industry, as other companies in our industry may calculate non-GAAP financial results differently, particularly related to non-recurring, unusual items. Our adjusted EBITDA is not a measurement of financial performance under GAAP, and should not be considered as an alternative to operating income or as an indication of operating performance or any other measure of performance derived in accordance with GAAP. We do not consider adjusted EBITDA to be a substitute for, or superior to, the information provided by GAAP financial results.

	For The Three Month Periods ended June 30,		For The Six Month Periods ended June 30,	
	2019	2018	2019	2018
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)
Depreciation and amortization	432,452	274,736	886,982	528,494
Amortization of debt discount	6,266	-	6,266	24,830
Amortization of deferred gain	(16,478)	(28,837)	(32,957)	(57,675)
Impairment of goodwill	1,988,701	-	1,988,701	-
Stock-based compensation expense	157,807	124,816	325,283	160,133
Interest expense	53,013	-	59,281	55,661
Provision (benefit) for income taxes	558,072	555,629	(543,839)	772,752
Adjusted EBITDA	<u>\$ 1,585,200</u>	<u>\$ (576,478)</u>	<u>\$ 150,354</u>	<u>\$ (813,045)</u>

### Adjusted EPS

Adjusted EPS excludes the impact of certain items and, therefore, has not been calculated in accordance with GAAP. We believe that exclusion of certain selected items assists in providing a more complete understanding of our underlying results and trends and allows for comparability with our peer company index and industry. We use this measure along with the corresponding GAAP financial measures to manage our business and to evaluate our performance compared to prior periods and the marketplace. The Company defines Non-GAAP (loss) income attributable to common stockholders as (loss) or income before amortization, stock-based compensation, expenses related to discontinued operations, impairment of long-lived assets and non-recurring acquisition costs. Adjusted EPS expresses adjusted (loss) income on a per share basis using weighted average diluted shares outstanding.

Adjusted EPS is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. These non-GAAP financial measures may not be computed in the same manner as similarly titled measures used by other companies. We expect to continue to incur expenses similar to the adjusted income from continuing operations and adjusted EPS financial adjustments described above, and investors should not infer from our presentation of these non-GAAP financial measures that these costs are unusual, infrequent or non-recurring.

The following table sets-forth Non-GAAP income (loss) attributable to common stockholders and basic and diluted earnings per share:

	For The Three Month Periods ended June 30,		For The Six Month Periods ended June 30,	
	2019	2018	2019	2018
Net loss attributable to common stockholders	\$ (1,594,633)	\$ (1,502,822)	\$ (2,539,363)	\$ (2,297,240)
Amortization of intangibles	269,151	98,660	618,570	197,326
Impairment of goodwill	1,988,701	-	1,988,701	-
Stock-based compensation expense	157,807	124,816	325,283	160,133
Non-GAAP net income (loss) attributable to common stockholders	\$ 821,026	\$ (1,279,346)	\$ 393,191	\$ (1,939,781)
Non-GAAP net income (loss) per share attributable to common stockholders:				
Basic	\$ 0.06	\$ (0.10)	\$ 0.03	\$ (0.17)
Diluted	\$ 0.06	\$ (0.10)	\$ 0.03	\$ (0.17)
Weighted average common shares outstanding:				
Basic	14,442,291	12,773,419	14,341,560	11,464,246
Diluted	14,916,460	12,773,419	14,815,730	11,464,246

Free cash flow, a non-GAAP measure for reporting cash flow, is defined as cash provided by or used in operating activities less capital expenditures for property and equipment, which includes capitalized software development costs. We believe free cash flow provides investors with an important perspective on cash available for investments and acquisitions after making capital investments required to support ongoing business operations and long-term value creation. We believe that trends in our free cash flow can be valuable indicators of our operating performance and liquidity.

Free cash flow is a non-GAAP financial measure and should not be considered in isolation or as a substitute for financial information provided in accordance with GAAP. This non-GAAP financial measure may not be computed in the same manner as similarly titled measures used by other companies.

We expect to continue to incur expenditures similar to the free cash flow adjustments described above, and investors should not infer from our presentation of this non-GAAP financial measure that these expenditures reflect all of our obligations which require cash. The following table reconciles cash provided by or used in operating activities, the most directly comparable GAAP financial measure, to free cash flow:

Cash flow:	For The Six Months Ended June 30,		Change
	2019	2018	
Cash provided by (used in) operating activities	\$ 1,713,884	\$ (3,848,089)	\$ 5,561,973
Capital expenditures	(1,356,975)	(60,210)	(1,296,765)
Free cash flow	\$ 356,909	\$ (3,908,299)	\$ 4,265,208

## Comparison of the three and six month periods ended June 30, 2019 and 2018

Revenues, Cost of Revenues and Gross Margin:

Entity:	For the Three Months Ended June 30, 2019				For the Three Months Ended June 30, 2018			
	Revenue	Cost of Revenue	Gross Margin	Gross Margin %	Revenue	Cost of Revenue	Gross Margin	Gross Margin %
OSS - (organic, inclusive of SkyScale)	\$ 10,007,805	\$ 5,712,191	\$ 4,295,614	42.9%	\$ 5,892,666	\$ 4,252,484	\$ 1,640,182	27.8%
Concept Development Inc.	894,561	717,717	176,844	19.8%	-	-	-	0.0%
Bressner Technology GmbH	3,983,870	3,043,170	940,700	23.6%	-	-	-	0.0%
	<u>\$ 14,886,236</u>	<u>\$ 9,473,078</u>	<u>\$ 5,413,158</u>	<u>36.4%</u>	<u>\$ 5,892,666</u>	<u>\$ 4,252,484</u>	<u>\$ 1,640,182</u>	<u>27.8%</u>

  

Entity:	For the Six Months Ended June 30, 2019				For the Six Months Ended June 30, 2018			
	Revenue	Cost of Revenue	Gross Margin	Gross Margin %	Revenue	Cost of Revenue	Gross Margin	Gross Margin %
OSS - (organic, inclusive of SkyScale)	\$ 15,237,891	\$ 9,441,094	\$ 5,796,797	38.0%	\$ 13,012,378	\$ 9,159,330	\$ 3,853,048	29.6%
Concept Development Inc.	1,194,015	1,063,444	130,571	10.9%	-	-	-	0.0%
Bressner Technology GmbH	8,512,229	6,614,816	1,897,413	22.3%	-	-	-	0.0%
	<u>\$ 24,944,135</u>	<u>\$ 17,119,354</u>	<u>\$ 7,824,781</u>	<u>31.4%</u>	<u>\$ 13,012,378</u>	<u>\$ 9,159,330</u>	<u>\$ 3,853,048</u>	<u>29.6%</u>

### Revenue

For the three month period ended June 30, 2019, total revenue increased \$8,993,570 or 152.6%, as compared to the same period in 2018. The increase in revenue was primarily driven by revenue from acquisitions which provided \$4,878,432 of which Bressner contributed \$3,983,870 or 67.6 percentage points and CDI contributed \$894,562 or 15.2 percentage points of the total increase in revenue. OSS saw an organic increase in revenue of \$4,133,652 or 70.1 percentage points as compared to same period in the prior year. The majority of this increase is attributable to shipments associated with our flash arrays on our airborne military flash contract as well as improvements in our sales of media and entertainment products. There was also a small decrease of \$18,514 or 0.3 percentage points attributable to SkyScale which has been dissolved.

For the six month period ended June 30, 2019, total revenue increased \$11,931,757 or 91.7%, as compared to the same period in 2018. The increase in revenue was primarily driven by revenue from acquisitions which provided \$9,706,245 of which Bressner contributed \$8,512,229 or 65.4 percentage points and CDI contributed \$1,194,016 or 9.2 percentage points of the total increase in revenue. OSS saw an increase in organic revenue of \$2,256,399 or 17.3 percentage points as compared to same period in the prior year. The majority of this increase is attributable to shipments associated with our flash arrays on our airborne military flash contract as well as improvements in our sales of media and entertainment products. There was also a small decrease of \$30,887 or a decrease of 0.2 percentage points attributable to SkyScale which has been dissolved.

### Cost of revenue and gross margin

Cost of revenue increased by \$5,220,594 or 122.7%, for the three month period ended June 30, 2019 as compared to the same period in 2018. The increase in cost of revenue was primarily driven by cost of revenue from acquisitions which contributed \$3,760,887 of which Bressner contributed \$3,043,170 or 71.5 percentage points and CDI contributed \$717,717 or 16.9 percentage points of the total increase in cost of revenue. OSS saw an increase in cost of revenue of \$1,626,461 or 38.2 percentage points as compared to same period in the prior year. The majority of this increase is attributable to a shipments associated with our flash arrays on our airborne military flash contract. There was also a decrease of \$166,754 or 3.9 percentage points attributable to SkyScale which has been dissolved.

The overall gross margin percentage increased from 27.8% for the three month period ended June 30, 2018 to 36.4% for the three month period ended June 30, 2019, an increase of 8.6 percentage points. OSS gross margin percentage for the three month period ended June 30, 2019 was 42.9%, which was 15.1 percentage points more in comparison to the prior year period of 27.8%. The 15.1 percentage point increase is attributable to a change in mix attributable to higher sales of our flash array systems. CDI contributed gross margin at a rate of 19.8%, while Bressner contributed gross margin at a rate of 23.6%.

Cost of revenue increased by \$7,960,024 or 86.9%, for the six month period ended June 30, 2019 as compared to the same period in 2018. The increase in cost of revenue was primarily driven by cost of revenue from acquisitions which contributed \$7,678,259 of which Bressner contributed \$6,614,815 or 72.2 percentage points and CDI contributed \$1,063,444 or 11.6 percentage points of the total increase in cost of revenue. OSS saw a minor increase in cost of revenue of \$281,765 or 3.1 percentage points as compared to same period in the prior year. The majority of this increase is attributable to in shipments associated with our flash arrays on our airborne military flash contract.

The overall gross margin percentage increased from 29.6% for the six month period ended June 30, 2018 to 31.4% for the six month period ended June 30, 2019, an increase of 1.8 percentage points. OSS gross margin percentage for the six month period ended June 30, 2019 was 38.0%, which was 8.4 percentage points more in comparison to the prior year period of 29.6%. The 8.4 percentage point increase is attributable to change in mix attributable to higher sales of our flash array systems. CDI contributed gross margin at a rate of 10.9% due to cost overruns on fixed price contracts during the first quarter of 2019, while Bressner contributed gross margin at a rate of 22.3%.

#### Operating expenses

##### *General and administrative expense*

General and administrative expense increased \$2,833,926 or 258.2%, for the three month period ended June 30, 2019 as compared to same period in 2018. OSS contributed an additional \$300,441 or 10.6% of the total annual increase in these expenses. The increase in general and administrative expense increased primarily due to third party service costs associated with being a public company which includes legal and accounting costs, insurance, listing fees and reporting and compliance costs. There was a reduction of \$64,199 or (2.3%) as a result of the dissolution of SkyScale. CDI contributed \$2,133,821 or 74.6% of which \$1,988,701 is attributable to impairment of goodwill due to a short-fall in the actual overall financial performance of CDI as compared to plan, a recurring need for working capital, and a decrease in the Company's stock price. Bressner contributed \$483,863 or 17.1% of the total annual increase. Overall general and administrative expenses increased as a percentage of revenue to 26.4% during the three month periods ended June 30, 2019 as compared to 18.6% during the same period in 2018.

General and administrative expense increased \$3,804,813 or 175.3%, for the six month period ended June 30, 2019 as compared to same period in 2018. OSS contributed an additional \$1,054,977 or 27.7% of the total annual increase in these expenses. The increase in general and administrative expense increased primarily due to third party service costs associated with being a public company which includes legal and accounting costs, insurance, listing fees and reporting and compliance costs. There was a reduction of \$580,064 or (15.2%) as a result of the dissolution of SkyScale. CDI contributed \$2,297,319 or 60.4% of which \$1,988,701 is attributable to impairment of goodwill due to a short-fall in the actual overall financial performance of CDI as compared to plan, a recurring need for working capital, and a decrease in the Company's stock price. Bressner contributed \$1,032,581 or 27.1% of the total annual increase. Overall general and administrative expenses increased as a percentage of revenue to 24.0% during the six month periods ended June 30, 2019 as compared to 16.7% during the same period in 2018.

##### *Marketing and selling expense*

Marketing and selling expense increased \$534,529 or 76.1% during the three month periods ended June 30, 2019 as compared to the same period in 2018. OSS had an increase of \$257,158 or 48.1% of the total increase. The major of the increase is attributable to an increase in external commissions associated with increased sales of flash array systems. There was a reduction in marketing and selling expense of \$37,040 or (6.9%) as a result of the dissolution of SkyScale. CDI's marketing expense for the three month period ended June 30, 2019 increased \$16,597 or 3.1%, and Bressner contributed \$297,814 or 55.7% of the total annual increase. Overall, total marketing and selling expense decreased as a percentage of revenue to 8.3% during the three month period ended June 30, 2019 as compared to 11.9% during the same period in 2018.

Marketing and selling expense increased \$803,447 or 51.1% during the six month periods ended June 30, 2019 as compared to the same period in 2018. OSS had an increase of \$217,308 or 27.0% of the total increase. The major increase was attributable to external commissions associated with the increase in sales of flash array systems. There was a reduction in marketing and selling expense of \$77,139 or (9.5%) as a result of the dissolution of SkyScale. CDI's marketing expense for the six month period ended June 30, 2019 increased \$18,804 or 2.3%, and Bressner contributed \$644,474 or 80.2% of the total annual increase. Overall, total marketing and selling expense decreased as a percentage of revenue to 9.5% during the six month period ended June 30, 2019 as compared to 12.1% during the same period in 2018.

#### *Research and development expense*

Research and development expense increased by \$266,382 or 27.8% during the three month period ended June 30, 2019 as compared to same period in 2018. These expenses are mainly comprised of salary and related costs and professional consulting services attributable to continued development of new and enhanced product offerings. OSS saw an increase of \$25,782 or 9.6%. The increase was largely driven by increased employee compensation costs. CDI contributed \$148,558 or 55.8% of the annual increase while Bressner contributed \$92,042 or 34.6% of the annual increase for 2019. Overall, total research and development expense decreased as a percentage of revenue to 8.2% during the three month period ended June 30, 2019 as compared to 16.3% during the same period in 2018.

Research and development expense increased by \$555,715 or 28.8% during the six month period ended June 30, 2019 as compared to same period in 2018. These expenses are mainly comprised of salary and related costs and professional consulting services attributable to continued development of new and enhanced product offerings. OSS saw an increase of \$92,332 or 16.6%. The increase was largely driven by increased employee compensation costs. CDI contributed \$275,830 or 49.6% of the annual increase while Bressner contributed \$187,553 or 33.8% of the annual increase for 2019. Overall, total research and development expense decreased as a percentage of revenue to 10.0% during the six month period ended June 30, 2019 as compared to 14.8% during the same period in 2018.

#### Interest expense

Interest expense increased \$53,013 or 100% for the three month period ended June 30, 2019 as compared to same period in 2018, as the outstanding debt associated with OSS which was outstanding as of June 30, 2018, was paid down in its entirety with proceeds from its public offering. On April 4, 2019, the Company borrowed \$1,500,000 from individuals and related parties at an annual interest rate of 9.5%, additionally, warrants of 10% of the value of the borrowing were also granted. The fair value of the warrants is amortized over the life of the loans and such costs are included as interest expense. On October 31, 2018, the Company acquired Bressner which has lines of credit and certain term loans outstanding and as a result incurred interest charges of \$11,610.

Interest expense increased \$3,620 or 6.5% for the six month period ended June 30, 2019 as compared to same period in 2018, as the outstanding debt associated with OSS which was outstanding as of June 30, 2018, was paid down in its entirety with proceeds from its public offering. On April 4, 2019, the Company borrowed \$1,500,000 from individuals and related parties at an annual interest rate of 9.5%, additionally, warrants of 10% of the value of the borrowing were also granted. The fair value of the warrants is amortized over the life of the loans and such costs are included as interest expense. On October 31, 2018, the Company acquired Bressner which has a line of credit and certain term loans outstanding and as a result incurred interest charges of \$17,827.

#### Other income (expense), net

Other income (expense), decreased \$57,498 or (105.6%) during the three month period ended June 30, 2019 as compared to the same period in 2018 of which \$27,045 of the reduction is attributable to OSS and SkyScale. In the prior year, OSS had other income attributable to settlement of certain outstanding obligations which did not occur in the current year. Additionally, Bressner had other expenses of \$30,978 with minor other income from CDI of \$525.

Other income (expense), decreased \$133,271 or (109.2%) during the six month period ended June 30, 2019 as compared to the same period in 2018 of which \$112,732 of the reduction is attributable to OSS. In the prior year OSS had other income attributable to settlement of certain outstanding obligations which did not occur in the current year.

Additionally, Bressner had other expenses of \$21,263 with minor other income from CDI of \$724.

#### Provision for income taxes

We have recorded an income tax provision and benefit of \$558,072 and \$543,839 for the three and six month periods ended June 30, 2019 as compared to a tax provision of \$555,629 and \$722,752 for the same periods in 2018. This benefit is attributable to projected annual taxable income for 2019 with a projected tax rate of 49.7%. The projected effective tax rate for the quarter differs from the statutory rate mainly due to permanent non-deductible goodwill amortization for Bressner Technology GmbH, as well as projecting federal, foreign and state tax liabilities for the year.

During the three month period ended June 30, 2019 and 2018 and the six month period ended June 30, 2018, the Company recorded a tax expense despite the fact that the Company experienced a pretax loss for those periods. In determining the periodic income tax expense, GAAP required us to forecast our annual effective income tax rate ("AETR") for the years December 31, 2019 and 2018. Based on management's projections, the Company expected income tax benefits related to research and development credits and equity compensation benefits to exceed our pretax earnings in 2019 and 2018. As a result, the Company expected its AETR to be negative for the year ended December 31, 2019, and when this negative AETR is applied to our quarterly pretax loss, the result is a quarterly income tax expense.

#### **Liquidity and capital resources**

During the six month period ended June 30, 2019, our primary sources of liquidity came from existing cash and third party borrowings. In addition to expected cash generated from operations, certain members of the Company's Board of Directors have executed definitive agreements to commit funds of up to \$4,000,000 as a credit facility, of which, the Company has borrowed \$1,500,000 from members of the Board of Directors and multiple parties for operations, facility expansion and ERP implementation. The Company is also developing plans for cost containment to ensure that liquidity will be sufficient to meet our cash requirements for current operations through at least a period of the next twelve months. Additionally, the Company, through Bressner Technology GmbH, received lines of credit of €2,700,000 during the period and received term loans in the amount of €1,300,000 subsequent to June 30, 2019.

On May 15, 2019, the Company filed an S-3 prospectus with the Securities and Exchange Commission which became effective on June 19, 2019, and allows the Company to offer up to \$100,000,000 aggregate dollar amount of shares of its common stock or preferred stock, debt securities, warrants to purchase its common stock, preferred stock or debt securities, subscription rights to purchase its common stock, preferred stock or debt securities and/or units consisting of some or all of these securities, in any combination, together or separately, in one or more offerings, in amounts, at prices and on the terms that the Company will determine at the time of the offering and which will be set forth in a prospectus supplement and any related free writing prospectus.

On June 26, 2019, the Company filed a prospectus supplement relating to its common stock, par value \$0.0001 per share, whereby under the prospectus supplement the Company may offer and sell common stock having an aggregate offering price of up to \$10,000,000 through Noble Capital Markets, Inc., ("Noble") acting as the Company's agent. As such, the Company has entered into an Equity Distribution Agreement with Noble dated as of June 26, 2019.

As of July 31, 2019, the Company has sold 1,019,561 shares of common stock through this offering for total gross proceeds of \$1,773,332, which resulted in net proceeds to us of \$1,746,046, after deducting compensation payable to Noble of \$27,286.

Our future capital requirements will depend on many factors including our growth rate, the timing and extent of spending to support development efforts, the expansion of our sales and marketing, the timing of new product introductions and the continuing market acceptance of our products and services.

Management believes that the Company has sufficient liquidity to satisfy its anticipated cash requirements for at least the next twelve months. However, there can be no assurance that our operations will become profitable or that external sources of financing, including the issuance of debt and/or equity securities, will be available at times and on terms acceptable to us, or at all. The Company's management prepares budgets and monitors the financial results of the Company as a tool to align liquidity needs to the recurring business requirements.

We may be required to seek additional equity or debt financing. In the event that additional financing is required from outside sources, we may not be able to raise monies on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be adversely affected.

The following table summarizes our cash flows for the six month periods ended June 30, 2019 and 2018

Cash flows:	For The Six Months Ended June 30,	
	2019	2018
Net cash provided by (used in) operating activities	\$ 1,713,884	\$ (3,848,089)
Net cash used in investing activities	\$ (1,355,925)	\$ (60,210)
Net cash provided by financing activities	\$ 2,323,170	\$ 12,989,902

#### *Operating Activities*

During the six month period ended June 30, 2019 we generated \$1,713,884 in cash from operating activities, an increase in cash of \$5,561,973 when compared to the cash used in operating activities of \$3,848,089 during the same period in 2018. The increase in cash provided by operating activities was primarily a result of a reduction in working capital requirements of \$4,626,977, a reduction in net loss of \$242,123, and an increase in non-cash adjustments of \$934,996. Non-cash adjustments include increases of \$2,793,115 comprised of the loss attributable to Noncontrolling interest, unrealized gain on foreign currency transactions, impairment of goodwill, warranty reserves, amortization of deferred gain, and depreciation and amortization. These increases were offset by \$1,177,119 in decreases in non-cash adjustments attributable to deferred benefit for income taxes, gain on disposal of property and equipment, provision for bad debt, inventory reserves, amortization of debt discount, and stock-based compensation expense.

Working capital requirements decreased overall by \$4,626,977. The sources of working capital of \$6,396,236 were attributable to reductions in accounts receivable, prepaids and other assets, and increases in accounts payable and accrued expenses and other liabilities for the comparable period. These sources were offset by an increase in working capital due to increased inventory levels of \$1,769,259.

Our ability to generate cash from operations in future periods will depend in large part on our profitability, the rate and timing of collections of our accounts receivable, our inventory turns and our ability to manage other areas of working capital including accounts payable.

#### *Investing Activities*

During the six month period ended June 30, 2019, we used cash of \$1,355,925 in investing activities as compared to \$60,210 used during the same period in 2018, an increase of \$1,295,715. The net increase is primarily due to tenant improvements to our headquarter facility and software costs and external consulting costs associated with the implementation of our ERP system with the anticipation for completion by the end of the third quarter 2019. The renovation and expansion of our facility is complete. As such, excluding these two major projects, we do not anticipate any other significant purchases of equipment beyond that which is anticipated for use in the normal course of our core business activity. We are projecting to spend an additional \$200,000 over the next two quarters to complete our ERP project.

### Financing Activities

During the six month periods ended June 30, 2019 we generated \$2,323,170 from financing activities as compared to the cash generated of \$12,989,902 during the same period in 2018. During the six month period ended June 30, 2019, we raised \$1,500,000 from individuals and related parties through the issuance of notes payable that bear interest at an annual rate of 9.5% and are repaid through 24 months monthly installments. Bressner increased borrowing under its lines of credit for the purchase of inventories and also borrowed funds through term loans at interest rates of 2.125% - 2.150% that are repaid through monthly installments of up to 24 months. The Company received proceeds of \$21,149 for the exercise of warrants and stock options.

During six month period ended June 30, 2018, the Company received proceeds from the sale of common stock in our initial public offering of \$19,500,000 which was offset by our stock issuance costs for commissions and third party professional services. We also received \$59,150 from the exercise of warrants and stock options. With the proceeds from our initial public offering we paid off our line of credit and retired all outstanding debt obligations.

### Contractual obligations and commitments

The following table sets forth our non-cancellable contractual obligations as of June 30, 2019.

Contractual Obligations:	Total	Less than 1 year	1-3 years	3-5 years	More than 5 Years
Notes payable	\$ 3,192,006	\$ 2,293,533	\$ 898,473		\$ -
Operating leases	2,133,913	613,469	1,151,452	368,992	-
Total	\$ 5,325,919	\$ 2,907,002	\$ 2,049,925	\$ 368,992	\$ -

We have made certain indemnities, under which the Company may be required to make payments to an indemnified party, in relation to certain transactions. We indemnify our directors, officers, employees and agents to the maximum extent permitted under the laws of the State of Delaware. In connection with our facilities leases, we indemnify our lessors for certain claims arising from the use of our facilities. The duration of the indemnities varies, and in many cases is indefinite. These indemnities do not provide for any limitation of the maximum potential future payments we could be obligated to make. Historically, we have not been obligated to make any payments for these obligations and no liabilities have been recorded for these indemnities.

### Off balance sheet arrangements

Other than lease commitments incurred in the normal course of business and certain indemnification provisions, we do not have any off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets, or any obligation arising out of a material variable interest in an unconsolidated entity.

We do not have any majority-owned subsidiaries that are not consolidated in the financial statements. Additionally, we do not have an interest in, or relationships with, any special purpose entities.

### Stockholder transactions

Effective August 1, 2016, we entered into a management services agreement with a company owned by the former Chief Executive Officer of Magma. The agreement calls for payments of \$180,000 per year for the first two years paid in monthly installments. In year three the amount is reduced to \$37,500 for the year paid in monthly installments. Additionally, we granted 30,000 options in conjunction with execution of this agreement. Payments for the three month periods ended June 30, 2019 and 2018 were \$9,375 and \$45,000, respectively and \$18,750 and \$90,000 for the six month periods ended June 30, 2019 and 2018, respectively.

### Critical accounting policies and estimates

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (GAAP). The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Our actual results could differ from these estimates. The critical accounting estimates, assumptions and judgments that we believe have the most significant impact on our consolidated financial statements are described below.

## Revenue Recognition

On January 1, 2019, the Company adopted the new accounting standard update ASC 606, Revenue from Contracts with Customers, which superseded nearly all existing revenue recognition guidance under GAAP, to all contracts using the modified retrospective method. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the impact of the adoption of the new standard to be immaterial to its net income on an ongoing basis.

The Company's performance obligations are satisfied over time as work is performed or at a point in time. The majority of the Company's revenue is recognized at a point in time when products ship and control is transferred to the customer. The Company determines revenue recognition through the following steps: (1) identification of the contract with a customer; (2) identification of the performance obligations in the contract; (3) determination of the transaction price; (4) allocation of the transaction price to the performance obligations in the contract; and (5) recognition of revenue when, or as, a performance obligation is satisfied.

The Company's contracts are executed through a combination of written agreements along with purchase orders with all customers including certain general terms and conditions. Generally, purchase orders entail products, quantities and prices, which define the performance obligations of each party and are approved and accepted by the Company. The Company's contracts with customers do not include extended payment terms. Payment terms vary by contract type and type of customer and generally range from 30 to 60 days from invoice. Additionally, taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by the Company from a customer and deposited with the relevant government authority, are excluded from revenue.

The transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring goods or services to the customer adjusted for estimated variable consideration. Variable consideration may include discounts, rights of return, refunds, and other similar obligations. The Company allocates the transaction price to each distinct product and service based on its relative standalone selling price. The standalone selling price for products primarily involves the cost to produce the deliverable plus the anticipated margin and for services is estimated based on the Company's approved list price.

In the normal course of business, the Company does not accept product returns unless the items are defective as manufactured. The Company establishes provisions for estimated returns and warranties. In addition, the Company does not typically provide customers with the right to a refund and does not transact for noncash consideration.

Customer agreements include one vendor managed inventory program. The Company recognizes revenue under this arrangement when (i) risks of ownership have passed to the customer; (ii) the customer's commitment to purchase the goods is fixed; (iii) there is a fixed schedule for delivery of the goods that is reasonable and consistent with the customer's business purpose; (iv) the Company does not have any specific performance obligations such that the earning process is not complete; (v) the ordered goods have been segregated from the Company's inventory and are not subject to being used to fill other orders; and (vi) the product is complete and ready for shipment. Also such arrangement must be requested by the customer and the customer has explained a substantial business purpose for the arrangement. Management also considers whether the customer's custodial risks are insured and whether modifications to the Company's normal billing and credit terms were required.

Revenues on certain fixed-price contracts where we provide engineering services, prototypes and completed products are recognized over the contract term based on the percentage of completion or based upon milestones delivered that are provided during the period and compared to the total estimated development and milestone goals to be provided over the entire contract. These services require that we perform significant, extensive and complex design, development, modification or implementation of our customers' systems. Performance will often extend over long periods of time, and our right to receive future payment depends on our future performance in accordance with the agreement.

The percentage-of-completion methodology involves recognizing probable and reasonably estimable revenue using the percentage of services completed, on a current cumulative cost to estimate total cost basis, using a reasonably consistent profit margin over the period. Due to the long-term nature of these projects, developing the estimates of costs often requires significant judgment. Factors that must be considered in estimating the progress of work completed and ultimate cost of the projects include, but are not limited to, the availability of labor and labor productivity, the nature and complexity of the work to be performed and the impact of delayed performance. If changes occur in delivery, productivity or other factors used in developing the estimates of costs or revenues, we revise our cost and revenue estimates, which may result in increases or decreases in revenues and costs, and such revisions are reflected in earnings in the period in which the revision becomes known.

The Company offer customers extended warranties beyond the standard one-year warranty on the product. The customer can purchase extended warranties from one to five years, in the bronze, silver or gold categories. This entails hardware repair or replacement, shipping methods on how the warranties will be returned / delivered, response times and hours of operations to receive support.

The Company does have recourse with some of its suppliers that offer more than a one-year guarantee on parts, but this is not standard. The few that offer greater than a year warranty, the Company is able to cover the cost of the part from the manufacturer for the failed part. The amounts of these costs vary in a wide range, but are not material, due to the infrequency of failure.

#### Stock-Based Compensation

We measure and recognize compensation expense for all stock-based awards granted to our employees and other service providers, including stock options granted under our 2017 and 2015 Plans, based on the estimated fair value of the award. We use the Black-Scholes option pricing model to estimate the fair value of stock option awards granted under our 2017 and 2015 Plans. We recognize the fair value of stock options granted under our 2017 and 2015's Plan as stock-based compensation on a straight line basis over the requisite service period. We record expense net of anticipated forfeitures and adjust the annual expense based upon actual experience.

Compensation cost for stock awards, which include restricted stock units ("RSUs") is measured at the fair value on the grant date and recognized as expense, net of estimated forfeitures, over the related service period. The fair value of stock awards is based on the quoted price of our common stock on the grant date less the present value of expected dividends not received during the vesting period.

Our use of the Black-Scholes option pricing model requires the input of highly subjective assumptions, including the fair value of the underlying common stock, expected term of the option, expected volatility of the price of our common stock, risk-free interest rates and the expected dividend yield of our common stock. The assumptions used in our option pricing model represent management's best estimates. These estimates involve inherent uncertainties and the application of management's judgment. If factors change and different assumptions are used, our stock-based compensation expense could be materially different in the future.

These assumptions and estimates are as follows:

- **Fair Value of Common Stock.** While we were a privately-held company, our Board of Directors considered numerous objective and subjective factors to determine the fair value of our common stock at each grant date. These factors included, but were not limited to, (i) contemporaneous valuations of common stock performed by unrelated third-party specialists; (ii) the rights, preferences and privileges of our convertible preferred stock relative to those of our common stock; (iii) the lack of marketability of our common stock; (iv) developments in the business; (v) the likelihood of achieving a liquidity event, such as an IPO or a merger or acquisition of our business, given prevailing market conditions; and (vi) the market performance of comparable publicly traded companies. Since the completion of our IPO, we use the closing quoted price of our common stock on the date of grant.
- **Expected Term.** The expected term represents the period that our stock-based awards are expected to be outstanding. The expected term assumptions were determined based on the vesting terms and contractual lives of the options, using the simplified method.

- Expected Volatility. Since we do not have sufficient trading history of our common stock, the expected volatility was determined based on the historical stock volatilities of comparable companies. Comparable companies consist of public companies in our industry that is similar in size, stage of life cycle and financial leverage. We intend to continue to apply this process using the same or similar public companies until a sufficient amount of historical information regarding the volatility of our own share price becomes available, or unless circumstances change such that the identified companies are no longer similar to us, in which case, more suitable companies whose share prices are publicly available would be used in the calculation.
- Risk-Free Interest Rate. The risk-free interest rate is based on the implied yield available on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term on the options.
- Dividend Rate. We have never declared or paid any cash dividends and do not plan to pay cash dividends in the foreseeable future, and, therefore, use an expected dividend yield of zero.

We will continue to use judgment in evaluating the assumptions related to our stock-based compensation on a prospective basis. As we continue to accumulate additional data related to our common stock, we may refine our estimation process, which could materially impact our future stock-based compensation expense.

#### Inventory Valuation

We value our inventory at the lower of cost or its estimated net realizable value. We use the average cost method for purposes of determining cost, which approximates the first-in, first-out method. We write down inventory for excess and obsolescence based upon a review of historical usage and assumptions about future demand, product mix and possible alternative uses. Actual demand, product mix and alternative usage may be lower than those that we project and this difference could have a material adverse effect on our gross margin if inventory write-downs beyond those initially recorded become necessary. Alternatively, if actual demand, product mix and alternative usage are more favorable than those we estimated at the time of such a write-down, our gross margin could be favorably impacted in future periods.

#### Goodwill, Intangible Assets and Long-lived Assets

We evaluate our goodwill, intangible and long-lived assets for impairment when events or circumstances arise that indicate our goodwill, intangible and long-lived assets may be impaired. Indicators of impairment include, but are not limited to, a significant deterioration in overall economic conditions, a decline in our market capitalization, the loss of significant business, significant decreases in funding for our contracts, or other significant adverse changes in industry or market conditions.

#### Income Taxes

The determination of income tax expense requires us to make certain estimates and judgments concerning the calculation of deferred tax assets and liabilities, as well as the deductions and credits that are available to reduce taxable income. We recognize deferred tax assets and liabilities for the expected future tax consequences of events that have been included in our consolidated financial statements. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates for the year in which the differences are expected to reverse.

In evaluating our ability to recover deferred tax assets, we consider all available positive and negative evidence, including our past operating results, our forecast of future earnings, future taxable income, and tax planning strategies. The assumptions utilized in determining future taxable income require significant judgment. We record a valuation allowance against deferred tax assets if, based upon the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. If it becomes more likely than not that a tax asset will be used for which a reserve has been provided, we reverse the related valuation allowance. If our actual future taxable income by tax jurisdiction differs from estimates, additional allowances or reversals of reserves may be necessary.

We use a two-step approach to recognize and measure uncertain tax positions. First, the tax position must be evaluated to determine the likelihood that it will be sustained upon external examination. If the tax position is deemed more-likely-than-not to be sustained, the tax position is then assessed to determine the amount of benefit to recognize in the financial statements. The amount of the benefit that may be recognized is the largest amount that has a greater than 50% likelihood of being realized upon ultimate settlement. We reevaluate our uncertain tax positions on a quarterly basis and any changes to these positions as a result of tax audits, tax laws or other facts and circumstances could result in additional charges to operations.

#### Business Combinations

We utilize the acquisition method of accounting for business combinations and allocate the purchase price of an acquisition to the various tangible and intangible assets acquired and liabilities assumed based on their estimated fair values. We primarily establish fair value using the income approach based upon a discounted cash flow model. The income approach requires the use of many assumptions and estimates including future revenues and expenses, as well as discount factors and income tax rates. Other estimates include:

- Estimated step-ups or write-downs for fixed assets and inventory;
- Estimated fair values of intangible assets; and
- Estimated income tax assets and liabilities assumed from the target

While we use our best estimates and assumptions as part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business acquisition date, our estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally no longer than one year from the business acquisition date, we record adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill.

For changes in the valuation of intangible assets between preliminary and final purchase price allocation, the related amortization is adjusted in the period it occurs. Subsequent to the purchase price allocation period any adjustment to assets acquired or liabilities assumed is included in operating results in the period in which the adjustment is determined. Should we issue shares of our common stock in an acquisition, we will be required to estimate the fair value of the shares issued.

#### **Recent accounting pronouncements**

Per the Company's consolidated financial statements Note 2 – Significant Accounting Policies, we may be implementing a number of changes, as required by FASB. See Note 2 for further details.

#### **Recently implemented accounting pronouncements**

Per the Company's consolidated financial statements Note 2 – Significant Accounting Policies, we have implemented a number of changes, as required by FASB. See Note 2 for further details.

#### **Interest rate risk**

Our exposure to interest rate risk is primarily associated with borrowing on revolving lines of credit denominated in both U.S. dollars and Euros. We are exposed to the impact of interest rate changes primarily through our borrowing activities for our variable rate borrowings.

#### **Concentration of credit risk**

Financial instruments that potentially expose us to concentrations of credit risk consist principally of cash, cash equivalents and accounts receivable. We place our cash and cash equivalents with financial institutions with high credit quality. At June 30, 2019 and December 31, 2018, we had \$4,944,853 and \$2,272,256 respectively, of cash and cash equivalents on deposit or invested with our financial and lending institutions.

We provide credit to our customers in the normal course of business. We perform ongoing credit evaluations of our customers' financial condition and limit the amount of credit extended when deemed necessary.

#### **Foreign currency risk**

We operate primarily in the United States. Foreign sales of products and services are primarily denominated in U.S. dollars. We also conduct business outside the United States through our foreign subsidiary in Germany, where business is largely transacted in non-U.S. dollar currencies particularly the Euro, which is subject to fluctuations due to changes in foreign currency exchange rates. Accordingly, we are subject to exposure from changes in the exchange rates of local currencies. Foreign currency transaction gains and losses are recorded in other income (expense), net in the consolidated statements of operations

OSS GmbH operates as an extension of OSS's domestic operations and acquired Bressner Technology GmbH in October 2018. The functional currency of OSS GmbH is the Euro. Transactions denominated in currencies other than the functional currency are remeasured to the functional currency at the average exchange rate in effect during the period. At the end of each reporting period, monetary assets and liabilities are translated using exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are remeasured at historical exchange rates. Consequently, changes in the exchange rates of the currencies may impact the translation of the foreign subsidiaries' statements of operations into U.S. dollars, which may in turn affect our consolidated statement of operations. The resulting foreign currency translation adjustments are recorded as a separate component of accumulated other comprehensive income in the consolidated statement of comprehensive income.

#### **Derivative Financial Instruments**

We employ derivatives to manage certain market risks through the use of foreign exchange forward contracts. We do not use derivatives for trading or speculative purposes. Our derivatives are designated as a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). We hedge a portion of the exchange risk involved in anticipation of highly probable foreign currency-denominated transactions. In anticipation of these transactions, we enter into foreign exchange contracts to provide currency at a fixed rate.

#### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

Not Applicable.

#### **Item 4. Controls and Procedures**

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure.

#### ***Limitation on Effectiveness of Controls***

Any control system, no matter how well designed and operated, can provide only reasonable assurance as to the tested objectives. The design of any control system is based in part upon 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, regardless of how remote. The inherent limitations in any control system include the realities that judgments related to decision-making can be faulty, and that reduced effectiveness in controls can occur because of simple errors or mistakes. Due to the inherent limitations in a cost-effective control system, misstatements due to error may occur and may not be detected.

### ***Evaluation of Disclosure Controls and Procedures***

Management is required to evaluate our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”). Disclosure controls and procedures are controls and other procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include controls and procedures designed to provide reasonable assurance that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer as appropriate to allow timely decisions regarding required disclosure. Based on our management’s evaluation (with the participation of our principal executive officer and principal financial officer), our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) were effective at a reasonable assurance level as of the end of the period covered by this report.

### ***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2019, which were identified in connection with management’s evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

## PART II—OTHER INFORMATION

### Item 1. Legal Proceedings.

We are subject to litigation, claims, investigations and audits arising from time to time in the ordinary course of our business. However, at this time, we are not aware of any pending, threatened, or unasserted claims.

### Item 1A. Risk Factors.

You should carefully review and consider the information regarding certain factors that could materially affect our business, financial condition or future results set forth under Item 1A (Risk Factors) in our Annual Report on Form 10-K for the year ended December 31, 2018. There have been no material changes from the factors disclosed in our 2018 Annual Report on Form 10-K filed on March 21, 2019, although we may disclose changes to such factors or disclose additional factors from time to time in our future filings with the Securities and Exchange Commission.

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

On April 4, 2019, the Company issued 69,766 warrants in conjunction with the issuance of \$1,500,000 in notes payable to individuals and related parties that vest upon issuance. The warrants allow for the purchase of the Company's common stock, par value \$0.0001 at \$2.15 per share.

### Item 3. Defaults Upon Senior Securities.

None.

### Item 4. Mine Safety Disclosures.

Not Applicable.

### Item 5. Other Information.

None.

**Item 6. Exhibits.**

<b>Exhibit Number</b>	<b>Description</b>
10.1*	<a href="#">Form of Note and Warrant Purchase Agreement</a>
10.2*	<a href="#">Form of Secured Note</a>
10.3*	<a href="#">Form of Warrant</a>
10.4*	<a href="#">Form of Security Agreement</a>
10.5*†	<a href="#">Original Equipment Manufacturing and Supply Agreement, dated as of July 1, 2019</a>
31.1**	<a href="#">Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</a>
31.2**	<a href="#">Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</a>
32.1**	<a href="#">Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 **.</a>
32.2**	<a href="#">Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 **.</a>
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

† Portions of this exhibit have been redacted in compliance with Regulation S-K Item 601(b)(10).

\* Filed herewith.

\*\* These certifications are being furnished solely to accompany this quarterly report pursuant to 18 U.S.C. Section 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and are not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Company Name

Date: August 8, 2019

By: \_\_\_\_\_ /s/ Steve Cooper

**Steve Cooper**  
**Chief Executive Officer and President**  
**(Principal Executive Officer)**

Date: August 8, 2019

By: \_\_\_\_\_ /s/ John W. Morrison Jr.

**John W. Morrison Jr.**  
**Chief Financial Officer**  
**(Principal Financial and Accounting Officer)**

**ONE STOP SYSTEMS, INC.**  
**NOTE AND WARRANT PURCHASE AGREEMENT**

THIS NOTE AND WARRANT PURCHASE AGREEMENT (this “Agreement”) is made as of \_\_\_\_\_, 2019, by and among One Stop Systems, Inc., a Delaware corporation (the “Company”), and the investors listed on Exhibit A hereto who become signatories to this Agreement (each an “Investor” and, collectively, the “Investors”).

THE PARTIES HEREBY AGREE AS FOLLOWS:

1. Issuance of Notes and Warrants.

1.1 Issuance of Notes. Subject to the terms and conditions of this Agreement, at each Closing (as defined below), the Company shall issue and sell to each Investor participating in such Closing, a senior secured promissory note (each such note, a “Note” and collectively, the “Notes”) in the principal amount set forth opposite each such Investor’s name on Exhibit A attached hereto (the “Principal Amount”), against payment by such Investor to the Company of the Principal Amount. The Company may issue and sell Notes with an aggregate Principal Amount of up to \$2,000,000 under this Agreement. The Notes shall each be in substantially the form of Exhibit B attached hereto. The Notes shall be secured pursuant to that certain Security Agreement substantially in the form of Exhibit D attached hereto (the “Security Agreement”).

1.2 Issuance of Warrants. Subject to the terms and conditions of this Agreement, at each Closing (as defined below), the Company shall issue and deliver to each Investor participating in such Closing, a common stock purchase warrant (each such warrant, a “Warrant” and collectively, the “Warrants”, and together with the Notes and the shares of stock issuable upon exercise of the Warrants, the “Securities”) providing each Investor the right to purchase that number of shares of the Company’s common stock equal to ten percent (10%) of said Investor’s Note as “warrant coverage.” The Warrants shall be exercisable at a price per share of common stock equal to the closing price of the Company’s stock the day immediately prior to such Closing. The Warrants shall each be in substantially the form of Exhibit C attached hereto, except as may otherwise be agreed upon by the Company and an Investor.

2. Closings.

2.1 Initial Closing. The initial closing of the purchase and sale of the Securities shall take place remotely via exchange of funds and documents, on \_\_\_\_\_, 2019 or such other time as the parties mutually agree (the “Initial Closing”).

2.2 Subsequent Closings. Subsequent to the Initial Closing, until such time as the aggregate Principal Amount evidenced by all of the Notes equals a total of \$2,000,000, the Company may sell additional Securities to such persons or entities as determined by the Company (each such closing, a “Subsequent Closing” and, together with the Initial Closing, each a “Closing”). For purposes of this Agreement, and all other agreements contemplated hereby, any additional purchaser so acquiring the Securities shall be deemed to be an “Investor” for purposes of this Agreement, and any Securities so acquired by such additional purchaser shall be deemed to be “Securities” for all purposes hereunder. Exhibit A shall be revised by the Company, without the consent of any other person or entity, to reflect the sale of Notes at all Subsequent Closings. The closing of the purchase and sale of such additional Securities hereunder shall take place on such date as is mutually agreeable to the Company and Investors that are identified on Exhibit A as purchasing Notes representing a majority of the aggregate Principal Amount of all Notes to be issued at such Subsequent Closing (or at such other time and place as is mutually agreed upon by the Company and such parties) (which each such date and place, together with the Initial Closing, are designated as a “Closing Date”).

2.3 Conditions of Investors' Obligations at Closing. The several obligations of each Investor to purchase the Notes on the date of the Initial Closing shall be subject to the prior or concurrent satisfaction of each of the conditions precedent set forth in this Section 2.3, any of which may be waived in writing by such Investor.

(a) Representations and Warranties. The representations and warranties made by the Company in Section 4 hereof shall be true and correct in all material respects on the Initial Closing date (except as to such representations and warranties made as of a specific date, which shall be measured as of such date).

(b) Conditions. All agreements and conditions contained in this Agreement to be performed by the Company on or prior to the Closing shall have been performed or complied with in all material respects.

2.4 Conditions of the Company's Obligations at Closing. The obligations of the Company to sell and issue Notes to each Investor at a Closing shall be subject to the prior or concurrent satisfaction of each of the conditions precedent set forth in this Section 2.4, any of which may be waived in writing by the Company.

(a) Representations and Warranties. The representations and warranties of such Investors contained in Section 3 of this Agreement shall be true and correct in all material respects on and as of each Closing, with the same effect as if made on and as of the Closing.

(b) Conditions. All agreements and conditions contained in this Agreement to be performed by the Investor on or prior to the Closing shall have been performed or complied with in all material respects.

2.5 Delivery. At each Closing, the Company shall deliver to each Investor (a) a Note in the Principal Amount designated opposite such Investor's name on Exhibit A, (b) a Warrant exercisable by the Investor to purchase such shares of the Company's common stock designated opposite such Investor's name on Exhibit A corresponding to the Principal Amount of Notes purchased by such Investor, and (c) a Security Agreement in the name of Investor, against delivery of (1) payment of the purchase price therefor by a wire transfer of immediately available funds, to a bank designated by the Company, and (2) delivery of counterpart signature pages to this Agreement and the Security Agreement (together with the Note and the Warrant, the "Transaction Documents").

3. Representations, Warranties and Covenants of Investors. Each Investor, severally and not jointly, hereby represents, warrants and covenants to the Company as follows:

3.1 Purchase for Own Account. Such Investor represents that it is acquiring the Securities solely for investment for such Investor's own account and not as a nominee or agent, and not with a view to the resale or distribution of any part thereof, and that such Investor has no present intention of selling, granting any participation in, or otherwise distributing the same. The acquisition by such Investor of any of the Securities shall constitute confirmation of the representation by such Investor that such Investor does not have any contract, undertaking, agreement or arrangement with any person to sell, transfer or grant participations to such person or to any third person, with respect to any of the Securities.

3.2 Disclosure of Information. Such Investor has had an opportunity to discuss the terms of this offering and the Company's business, management and financial affairs with the Company's management, and the opportunity to inspect the Company's facilities and such books and records and material contracts as such Investor deemed necessary to its determination to purchase the Securities.

3.3 Investment Experience. Either (i) such Investor or its officers, directors, managers or controlling persons has a preexisting personal or business relationship with the Company or its officers, directors or controlling persons, or (ii) such Investor, by reason of its own business and financial experience, has the capacity to protect its own interests in connection with the investment contemplated hereby. Such Investor represents that it is an investor in securities of companies in the development stage and acknowledges that it is able to fend for itself, can bear the economic risk of its investment, and has such knowledge and experience in financial or business matters that it is capable of evaluating the merits and risks of the investment in the Securities.

3.4 Accredited Investor; Non-U.S. Persons. Such Investor either (a) is an “accredited investor” within the meaning of Securities and Exchange Commission (“SEC”) Rule 501 of Regulation D, as presently in effect, or (b) (i) certifies that such Investor is not a “U.S. person” within the meaning of SEC Rule 902 of Regulation S, as presently in effect, and that such Investor is not acquiring the Securities for the account or benefit of any such U.S. person, (ii) agrees to resell the Securities only in accordance with the provisions of Regulation S, pursuant to registration under the Act, or pursuant to an available exemption from registration and agrees not to engage in hedging transactions with regard to such Securities unless in compliance with the Act, (iii) agrees that any certificates for any Securities issued to such Investor shall contain a legend to the effect that transfer is prohibited except in accordance with the provisions of Regulation S, pursuant to registration under the Act or pursuant to an available exemption from registration and that hedging transactions involving such Securities may not be conducted unless in compliance with the Act, and (iv) agrees that the Company is hereby required to refuse to register any transfer of any Securities issued to such Investor not made in accordance with the provisions of Regulation S, pursuant to registration under the Act, or pursuant to an available exemption from registration.

3.5 Restrictions on Transfer. Such Investor understands that the Securities are characterized as “restricted securities” under the federal securities laws inasmuch as they are being acquired from the Company in a transaction not involving a public offering and that under such laws and applicable regulations such securities may be resold without registration under the Securities Act of 1933, as amended (the “Act”), only in certain limited circumstances. In this connection, such Investor represents that it is familiar with SEC Rule 144, as presently in effect, and understands the resale limitations imposed thereby and by the Act. Such Investor understands that the Securities have not been and will not be registered under the Act and have not been and will not be registered or qualified in any state in which they are offered, and thus the Investor will not be able to resell or otherwise transfer his, her or its Securities unless they are registered under the Act and registered or qualified under applicable state securities laws, or an exemption from such registration or qualification is available. Such Investor has no immediate need for liquidity in connection with this investment and does not anticipate that it will need to sell his, her or its Securities in the foreseeable future. INVESTOR UNDERSTANDS AND ACKNOWLEDGES HEREIN THAT AN INVESTMENT IN THE COMPANY’S SECURITIES INVOLVES AN EXTREMELY HIGH DEGREE OF RISK AND MAY RESULT IN A COMPLETE LOSS OF HIS, HER OR ITS INVESTMENT.

3.6 Further Limitations on Disposition. Without in any way limiting the representations set forth above, such Investor further agrees not to make any disposition of all or any portion of the Securities unless and until the transferee has agreed in writing for the benefit of the Company to be bound by this Section 3 and any other agreement that the purchasers of such Securities are required to execute and deliver in connection with the purchase of such Securities, and:

(a) there is then in effect a registration statement under the Act covering such proposed disposition and such disposition is made in accordance with such registration statement; or

(b) (i) such Investor shall have notified the Company of the proposed disposition and shall have furnished the Company with a detailed statement of the circumstances surrounding the proposed disposition, and (ii) if reasonably requested by the Company, such Investor shall have furnished the Company with an opinion of counsel reasonably satisfactory to the Company that such disposition will not require registration of such shares under the Act. It is agreed that the Company will not require opinions of counsel for transactions made pursuant to Rule 144.

Notwithstanding the provisions of subsections (a) and (b) above, no such registration statement or opinion of counsel shall be necessary for a transfer by an Investor that is a partnership or limited liability company to a partner of such partnership or a member of such limited liability company or a retired partner of such partnership who retires after the date hereof or a retired member of such limited liability company who retires after the date hereof, or to the estate of any Investor or the transfer by gift, will or intestate succession by any Investor to his or her spouse or to the siblings, lineal descendants or ancestors of such Investor or his or her spouse, if the transferee agrees in writing to be subject to the terms hereof to the same extent as if he or she were an original Investor hereunder.

3.7 Confidentiality. Such Investor agrees that he, she or it shall keep confidential and shall not use, disclose or divulge any information which such Investor may obtain from the Company, pursuant to financial statements, reports and other materials submitted by the Company as required hereunder or under any other documents, or pursuant to information rights granted to an Investor unless such information is known, or until such information becomes known, to the public through no fault of such Investor or its agents, or unless the Company's President or Chief Executive Officer gives written consent to such Investor's release of such information, except that no such written consent shall be required (and Investor shall be free to release such information) if such information is to be provided to such Investor's counsel or accountant, or to an officer, director, general partner, limited partner, shareholder, investment counselor or advisor, or employee of an Investor with a need to know such information; provided that any such counsel, accountant, officer, director, general partner, limited partner, shareholder, investment counselor or advisor, or employee shall be bound by the provisions of this Section 3.7. Notwithstanding the foregoing, this Section 3.7 shall not apply (a) to information which an Investor learns from a third party with the right to make such disclosure, provided Investor complies with the restrictions imposed by the third party, (b) to information which is in such Investor's possession prior to the time of disclosure by the Company and not acquired by Investor under a confidentiality obligation, (c) to the minimum extent Investor is required to disclose such information by law or a governmental regulatory authority, (d) to the minimum extent (after requesting and pursuing confidential treatment to the extent reasonably possible) such Investor is required to disclose such information by court order. For the purposes of this Agreement: (A) a Person shall be deemed an "Affiliate" of another Person who, directly or indirectly, controls, is controlled by or is under common control with such Person, including, without limitation, any general partner, managing member, officer or director of such Person or any venture capital fund now or hereafter existing that is controlled by one or more general partners or managing members of, or shares the same management company with, such Person; and (B) "Person" shall mean any individual, corporation (including any nonprofit corporation), general partnership, limited partnership, limited liability partnership, joint venture, estate, trust, company (including any limited liability company or joint stock company), firm or other enterprise, association, organization or entity, unincorporated organization or government or political subdivision thereof, or any other entity.

3.8 Investment Entity. Such Investor, if a corporation, partnership, trust or other entity, is authorized and otherwise duly qualified to purchase and hold the Securities; such entity has made its investment decision to purchase the Securities at its office address for Investor as set forth on the signature page hereto; and such entity has not been formed for the specific purpose of acquiring the Securities. Such Investor, if a natural person, resides in the state identified in the address of Investor set forth on the signature page hereto.

3.9 Validity. When executed and delivered by such Investor, and assuming execution and delivery by the Company, this Agreement constitutes such Investor's valid and legally binding obligations, enforceable in accordance with its respective terms except as may be limited by (i) applicable bankruptcy, insolvency, reorganization or other laws of general application relating to or affecting the enforcement of creditors' rights generally, and (ii) the effect of rules of law governing the availability of equitable remedies. Investor has full power and authority to enter into this Agreement and any and all consents required in connection herewith and the transactions contemplated hereby have been obtained.

3.10 No Tax Advice. Such Investor understands that such Investor may suffer adverse tax consequences as a result of such Investor's purchase or disposition of the Securities. Such Investor represents that he, she or it has consulted any tax consultants that such Investor deems advisable in connection with the purchase or disposition of the Securities and that such Investor is not relying on the Company or the Company's counsel for any tax advice.

4. Representations and Warranties of the Company. The Company hereby represents and warrants to each Investor that, at the Initial Closing:

4.1 Organization, Good Standing and Qualification. The Company is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all requisite corporate power and authority to carry on its business as now conducted.

4.2 Authorization. All action on the part of the Company necessary for the authorization, execution and delivery of this Agreement, the performance of all obligations of the Company hereunder, and the authorization, issuance (or reservation for issuance), sale and delivery of the Securities, has been taken or will be taken prior to each Closing. Each of the Transaction Documents to which the Company is a party constitutes the valid and legally binding obligation of the Company, enforceable against the Company in accordance with its terms, except (i) as limited by applicable bankruptcy, insolvency, reorganization, moratorium and other laws of general application affecting enforcement of creditors' rights generally, and (ii) as limited by laws relating to the availability of specific performance, injunctive relief or other equitable remedies.

4.3 Absence of Required Consents; No Violations. No consent, approval, order or authorization of, or registration, qualification, designation, declaration or filing with, any Governmental Authority on the part of the Company is required in connection with the consummation of the transactions contemplated by the Transaction Documents, except for such filing(s) pursuant to applicable federal or state securities laws as may be necessary, which filings will be timely effected after the relevant Closing. The Company is not in violation or default (i) of any provision of its Certificate of Incorporation or Bylaws, or (ii) in any material respect of any instrument, judgment, order, writ, decree or contract to which it is a party or by which it is bound, except in the case of this clause (ii) for such violations or defaults which could not reasonably be expected to result in a material adverse effect. The execution, delivery and performance of the Transaction Documents and the consummation of the transactions contemplated thereby will not result in any such violation or be in conflict with or constitute, with or without the passage of time and giving of notice, either a default under any such provision, instrument, judgment, order, writ, decree or contract.

4.4 Valid Issuance of Securities.

(a) The Securities, when issued, sold and delivered in accordance with the terms of this Agreement, will be duly and validly issued, fully paid, and nonassessable, and will be free of restrictions on transfer other than restrictions on transfer under this Agreement, and under applicable state and federal securities laws. The Common Stock issuable upon exercise of the Warrants will be duly and validly reserved for issuance upon the creation of such equity securities and, upon issuance in accordance with the terms of the Company's Certificate of Incorporation will be duly and validly issued, fully paid, nonassessable, and will be free of restrictions on transfer other than restrictions on transfer under this Agreement, and under applicable state and federal securities laws.

(b) No “bad actor” disqualifying event described in Rule 506(d)(1)(i)-(viii) of the Securities Act (a “Disqualification Event”) is applicable to the Company or, to the Company’s knowledge, any Company Covered Person, except for a Disqualification Event as to which Rule 506(d)(2)(ii-iv) or (d)(3), is applicable. “Company Covered Person” means, with respect to the Company as an “issuer” for purposes of Rule 506 promulgated under the Securities Act, any Person listed in the first paragraph of Rule 506(d)(1).

5. Legends.

5.1 Federal Legends. The stock certificates evidencing the Securities shall bear such restrictive legends as the Company and the Company’s counsel deem necessary or advisable under applicable law or pursuant to this Agreement, including, without limitation, the following:

“THE SECURITIES EVIDENCED HEREBY AND ANY SECURITIES INTO WHICH THIS SECURITY IS CONVERTIBLE HAVE BEEN ACQUIRED FOR INVESTMENT AND HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR QUALIFIED UNDER ANY STATE SECURITIES LAWS. SUCH SECURITIES MAY NOT BE SOLD OR OFFERED FOR SALE OR OTHERWISE DISTRIBUTED EXCEPT (I) IN CONJUNCTION WITH AN EFFECTIVE REGISTRATION STATEMENT FOR THE SECURITIES UNDER THE ACT, (II) IN COMPLIANCE WITH RULE 144, OR (III) PURSUANT TO AN OPINION OF COUNSEL, REASONABLY SATISFACTORY TO THE COMPANY, THAT SUCH REGISTRATION OR COMPLIANCE IS NOT REQUIRED AS TO SAID SALE, OFFER OR DISTRIBUTION.”

5.2 Other Legends. The Warrants and stock certificates evidencing the shares issuable upon exercise of the Warrants shall also bear any legend required by the Company’s Bylaws, or as may be required pursuant to any state, local, or foreign law governing such securities.

5.3 Refusal to Transfer. The Company shall not be required (i) to transfer on its books any Securities that have been sold or otherwise transferred in violation of any of the provisions of this Agreement, or (ii) to treat as owner of such Securities or to accord the right to vote or pay dividends to any purchaser or other transferee to whom such Securities shall have been so transferred.

6. Miscellaneous.

6.1 Successors and Assigns. Except as otherwise provided therein, the terms and conditions of this Agreement and the other Transaction Documents shall inure to the benefit of and be binding upon the respective successors and assigns of the parties (including transferees of any Securities); provided that the Company may not assign or transfer its rights or obligations hereunder or under the other Transaction Documents without the prior written consent of the holders of a majority of the aggregate Principal Amount under all Notes. The Securities shall be transferable upon obtaining the prior written consent of the Company and subject to compliance with applicable securities laws and Section 3. Nothing in this Agreement, express or implied, is intended to confer upon any party other than the parties hereto or their respective successors and assigns any rights, remedies, obligations, or liabilities under or by reason of this Agreement, except as expressly provided in this Agreement.

6.2 Governing Law. This Agreement and all acts and transactions pursuant hereto and the rights and obligations of the parties hereto shall be governed, construed and interpreted in accordance with the laws of the State of California, without giving effect to principles of conflicts of law.

6.3 Titles and Subtitles. The titles and subtitles used in this Agreement are used for convenience only and are not to be considered in construing or interpreting this Agreement.

6.4 Notices. Except as may be otherwise provided herein, all notices, requests, waivers and other communications made pursuant to this Agreement shall be in writing and shall be conclusively deemed to have been duly given (a) when hand delivered to the other party; (b) when sent by facsimile to the number set forth below if sent between 8:00 a.m. and 5:00 p.m. recipient's local time on a Business Day, or on the next Business Day if sent by facsimile to the number set forth below if sent other than between 8:00 a.m. and 5:00 p.m. recipient's local time on a Business Day; (c) three Business Days after deposit in the U.S. mail with first class or certified mail receipt requested postage prepaid and addressed to the other party at the address set forth below; or (d) the next Business Day after deposit with a national overnight delivery service, postage prepaid, addressed to the parties as set forth below with next Business Day delivery guaranteed, provided that the sending party receives a confirmation of delivery from the delivery service provider. Each Person making a communication hereunder by facsimile shall promptly confirm by telephone to the Person to whom such communication was addressed each communication made by it by facsimile pursuant hereto but the absence of such confirmation shall not affect the validity of any such communication. A party may change or supplement the addresses given above, or designate additional addresses, for purposes of this Section 6.4 by giving the other party written notice of the new address in the manner set forth above. "Business Day" shall mean any day other than a Saturday, Sunday, U.S. federal holiday or any other day upon which banks in New York and San Francisco are not open for business. Any communication to an Investor shall be sent to such Investor at the address set forth on the signature page hereto, and if to the Company, at the following address:

One Stop Systems, Inc.  
2235 Enterprise St., Suite #110  
Escondido, California 92029  
Email: \_\_\_\_\_

With a copy to (which such copy shall not constitute notice):

Attn: \_\_\_\_\_  
Email: \_\_\_\_\_

6.5 Amendments and Waivers. Any term of this Agreement may be amended or modified, and the observance of any term of this Agreement may be waived (either generally or in a particular instance and either retroactively or prospectively) only with the written consent of, or a written instrument signed by (x) the Company; and (y) Investors who, after the Closing, hold Notes in an aggregate Principal Amount equal to more than fifty-percent (50%) of the aggregate Principal Amount of all then outstanding Notes. Any waiver or amendment effected in accordance with this Section 6.5 shall be binding upon each holder of any Securities acquired under this Agreement at the time outstanding (including securities into which such Securities are convertible), each future holder of all such Securities, and the Company, and its and their respective successors and assigns. Notwithstanding the foregoing, the Company may unilaterally amend Exhibit A of this Agreement to the extent necessary to add new Investors at Subsequent Closings, in accordance with Section 2.2 of this Agreement.

6.6 Severability. In case any one or more of the provisions contained in this Agreement shall, for any reason, be judicially determined to be invalid, illegal or unenforceable in any respect, (i) the remaining terms and provisions hereof shall be unimpaired and shall remain in full force and effect, and (ii) the invalid or unenforceable provision or term shall be replaced by a term or provision that is valid and enforceable and that comes closest to expressing the intention of such invalid or unenforceable term or provision, and, if the foregoing provision of this clause (ii) is not permitted pursuant to applicable law, then (iii) this Agreement shall be construed as if such invalid, illegal or unenforceable provision had never been contained herein.

6.7 Finder's Fee. Each party represents that it neither is nor will be obligated for any finders' fee or commission in connection with this transaction.

6.8 Further Assurances. Each Investor and the Company shall from time to time and at all times hereafter make, do, execute, or cause or procure to be made, done and executed such further acts, deeds, conveyances, consents and assurances without further consideration, which may reasonably be required to effect the transactions contemplated by the Transaction Documents.

6.9 Survival of Representations Warranties and Covenants. The representations and warranties of the Company and the Investors contained in or made pursuant to this Agreement shall survive the execution and delivery of this Agreement and the Closing and shall in no way be affected by any investigation or knowledge of the subject matter thereof made by or on behalf of the Investors or the Company.

6.10 Separability. The obligations of each Investor under any Transaction Document are several and not joint with the obligations of any other Investor, and no Investor shall be responsible in any way for the performance of the obligations of any other Investor under any Transaction Document. Each Investor shall be responsible only for its own representations, warranties, agreements and covenants hereunder. Nothing contained herein or in any other Transaction Document, and no action taken by any Investor pursuant hereto or thereto, shall be deemed to constitute the Investors as a partnership, an association, a joint venture or any other kind of entity, or create a presumption that the Investors are in any way acting in concert or as a group with respect to such obligations or the transactions contemplated by the Transaction Documents. Except as otherwise provided in any Transaction Document, each Investor shall be entitled to independently protect and enforce its rights, including without limitation the rights arising out of this Agreement or out of the other Transaction Documents, and it shall not be necessary for any other Investor to be joined as an additional party in any proceeding for such purpose. Any invalidity, illegality or limitation on the enforceability of the Agreement or any part thereof, by any Investor, whether arising by reason of the law of the respective Investor's domicile or otherwise, shall in no way affect or impair the validity, legality or enforceability of this Agreement with respect to other Investors.

6.11 Acknowledgment. Each Investor acknowledges that: (a) he, she or it has read the Transaction Documents; (b) it has been represented in the preparation, negotiation and execution of the Transaction Documents by legal counsel of its own choice or has voluntarily declined to seek such counsel; and (c) it understands the terms and consequences of the Transaction Documents and is fully aware of the legal and binding effect of the Transaction Documents.

6.12 Construction. The Company and Investors have participated jointly in the negotiation and drafting of this Agreement. If an ambiguity or question of intent or interpretation arises, this Agreement shall be construed as if drafted jointly by the parties hereto and no presumption or burden of proof shall arise favoring or disfavoring any party because of the authorship of any provision of this Agreement. The words "include," "includes," and "including" shall be deemed to be followed by "without limitation." Pronouns in masculine, feminine, and neuter genders shall be construed to include any other gender, and words in the singular form shall be construed to include the plural and vice versa, unless the context otherwise requires. The words "this Agreement," "herein," "hereof," "hereby," "hereunder," and words of similar import refer to this Agreement as a whole and not to any particular subdivision unless expressly so limited. Any reference herein to "day" or "days" shall, unless otherwise provided for, mean a calendar day or calendar days.

6.13 Entire Agreement. This Agreement and the Transaction Documents (and the Exhibits hereto and thereto) constitute the entire understanding between the Company and the Investors relative to the subject matter hereof. Any prior and contemporaneous agreement, discussion, understanding, correspondence and/or communication between the Company and such Investors regarding the purchase of securities, capital stock of the Company or otherwise, whether written or oral, is superseded by this Agreement.

6.14 Attorney's Fees. If, in any action at law or in equity (including arbitration), it is necessary to enforce or interpret the terms of any of the Transaction Documents, the prevailing party shall be entitled to reasonable attorney's fees, costs and necessary disbursements in addition to any other relief that such party may be entitled.

6.15 Waiver of Conflicts. Each party to this Agreement acknowledges and agrees that Procopio, Cory, Hargreaves & Savitch LLP ("Procopio") is acting as counsel only to the Company in connection with the preparation of this Agreement and related securities offerings, and that Procopio has in the past represented, and may, now or in the future, represent the Company, and/or its affiliates in matters unrelated to the Company. The applicable rules of professional conduct require that Procopio inform the parties previously or presently represented by Procopio of this representation and obtain their consent. Procopio has served as counsel to the Company and has negotiated the terms of this Agreement and related securities offerings solely on behalf of the Company. Each party to this Agreement acknowledges, represents and warrants to Procopio that: (A) (i) the party has read this Agreement; (ii) the party has been represented in the preparation, negotiation and execution of this Agreement and related securities offerings by legal counsel of the party's own choice or has voluntarily declined to seek such counsel; and (iii) the party understands the terms and consequences of this Agreement and is fully aware of the legal and binding effect; and (B) the party understands that (i) Procopio has been retained by the Company in connection with the preparation, negotiation and execution of this Agreement and related securities offerings; and (ii) the party has not engaged the services of Procopio in connection with the preparation, negotiation and execution of this Agreement and related securities offerings and the party is not represented by Procopio in the preparation, negotiation and execution of this Agreement and related securities offerings.

6.16 Counterparts. This Agreement may be executed in two (2) or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument. Counterparts may be delivered via facsimile, electronic mail (including pdf or any electronic signature complying with the U.S. federal ESIGN Act of 2000, *e.g.*, [www.docusign.com](http://www.docusign.com)) or other transmission method and any counterpart so delivered shall be deemed to have been duly and validly delivered and be valid and effective for all purposes.

*[Signature Page Follows]*

IN WITNESS WHEREOF, the parties hereto have executed this Note and Warrant Purchase Agreement as of the date first above written.

**Company:**

**One Stop Systems, Inc.,**  
a Delaware corporation

By: \_\_\_\_\_  
John W. Morrison, Jr., Chief Financial Officer

**INVESTORS:**

**If Investor is a Corporation, Partnership or Other Entity:**

**If Investor is an Individual:**

\_\_\_\_\_  
*Name of Entity*

\_\_\_\_\_  
*Print Name of Individual*

\_\_\_\_\_  
*Signature of Authorized Person*

\_\_\_\_\_  
*Signature of Individual*

\_\_\_\_\_  
*Print Name of Authorized Person*

\_\_\_\_\_  
*Print Name of Individual (If more than one signatory)*

\_\_\_\_\_  
*Title*

\_\_\_\_\_  
*Signature of Individual (If more than one signatory)*

Telephone (Day): \_\_\_\_\_

Telephone (Day): \_\_\_\_\_

Facsimile: \_\_\_\_\_

Facsimile: \_\_\_\_\_

Email Address: \_\_\_\_\_

Email Address: \_\_\_\_\_

Address: \_\_\_\_\_

Address: \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

**EXHIBITS**

**Exhibits**

Exhibit A	Schedule of Investors
Exhibit B	Form of Note
Exhibit C	Form of Warrant
Exhibit D	Form of Security Agreement

**EXHIBIT A**

**Schedule Of Investors**

**Investor**

**Principal Amount of Note**

**Date of Purchase**

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**EXHIBIT B**

**Form Of Senior Secured Promissory Note**

[Attached]

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**EXHIBIT C**

**Form of Common Stock Purchase Warrant**

[Attached]

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**EXHIBIT D**

**Form of Security Agreement**

[Attached]

**SENIOR SECURED  
PROMISSORY NOTE**

**By**

**ONE STOP SYSTEMS, INC.  
("Payor")**

**In Favor Of**

\_\_\_\_\_  
**("Payee")**

\_\_\_\_\_, 20\_\_

**SENIOR SECURED PROMISSORY NOTE**

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Payor: One Stop Systems, Inc.  
2235 Enterprise St. #101  
Escondido, CA 92029

Payee: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

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Date of Note:	Principal Amount:	Interest Rate:	Due Date:
_____	\$ _____	9.5%	_____

**PROMISE TO PAY.** One Stop Systems, Inc., a Delaware corporation (“Payor”) promises to pay to \_\_\_\_\_ (“Payee”), in lawful money of the United States of America, the principal amount of \_\_\_\_\_ Dollars (\$ \_\_\_\_\_), together with interest on the unpaid principal balance on or before \_\_\_\_\_ (“Due Date”).

**PAYMENT.** Principal and interest will be payable in twenty-four (24) consecutive monthly fully amortized installments of \_\_\_\_\_ Dollars (\$ \_\_\_\_\_) on the fifteenth day of each month beginning \_\_\_\_\_. Such payments will continue until the entire indebtedness evidenced by this Note and all accrued and unpaid interest is fully paid, with any unpaid principal and interest due and payable on \_\_\_\_\_ (“Maturity Date”).

Each payment under this Note will be credited in the following order: (a) costs, fees, charges, and advances paid or incurred by Payee or payable to Payee and interest under any provision of this Note, in such order as Payee, in his sole and absolute discretion, elects, (b) interest payable under the Note, and (c) principal under the Note.

Payor will pay Payee at Payee’s address shown above or at such other place as Payee may designate in writing.

**FIXED INTEREST RATE.** The interest rate applied to the unpaid principal balance of this Promissory Note (“Note”) will be nine and one-half percent (9.5%) per annum. Interest will be calculated on the basis of a 365-day year.

**PREPAYMENT.** Payor may pay without penalty all or a portion of the amount owed earlier than it is due. Early payments will not, unless agreed to by Payee in writing, relieve Payor of its obligation to make payment of all principal and interest by the Due Date.

**DEFAULT.** Payor will be in default if it fails to make the payment when due and such failure continues for ten (10) days after written notice of default is deposited in the United States mail, with pre-paid first class postage.

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**PAYEE'S RIGHTS.** Upon default, Payee may declare the entire unpaid principal balance of this Note and all accrued unpaid interest immediately due, without notice, and then Payor will pay that amount. Upon Payor's failure to pay all amounts declared due pursuant to this section, including failure to pay upon final maturity, Payee, at its option, may also hire or pay someone else to help collect this Note if Payor does not pay. Payor will also pay Payee that amount. This includes, subject to any limits under applicable law, Payee's attorneys' fees and legal expenses whether or not there is a lawsuit, including attorneys' fees and legal expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Payor also will pay any court costs, in addition to all other sums provided by law. This Note has been delivered to Payee and accepted by Payee in the State of California. If there is a lawsuit, Payor agrees to submit to the jurisdiction of the courts of San Diego County, the State of California. This Note will be governed by and construed in accordance with the laws of the State of California.

**USURY.** All agreements between Payor and Payee are expressly limited, so in no event or contingency, whether because of the advancement of the proceeds of this Note, acceleration of maturity of the unpaid principal balance, or otherwise, will the amount paid or agreed to be paid to Payee for the use, forbearance, or retention of the money to be advanced under this Note exceed the highest lawful rate permissible under applicable usury laws. If, under any circumstances, fulfillment of any provision of this Note, after timely performance of such provision is due, will involve exceeding the limit of validity prescribed by law that a court of competent jurisdiction deems applicable, then, ipso facto, the obligations to be fulfilled will be reduced to the limit of such validity. If under any circumstances, Payee will ever receive as interest an amount exceeding the highest lawful rate, the amount that would be excessive interest will be applied to reduce the unpaid principal balance under this Note and not to pay interest, or, if such excessive interest exceeds the unpaid principal balance under this Note, such excess will be refunded to Payor. This provision will control every other provision of the Note.

**SENIOR SECURED NOTE.** The obligations of Payor hereunder are secured by a first priority security interest in the "Collateral" (as defined below) granted to Payee by the Payor hereunder pursuant to the terms and conditions of a Security Agreement of even date herewith between Payor and Payee. "Collateral" means all of Payor's right, title and interest in, to and under the Payor's assets and equipment, including titles to said assets (the "Pledged Assets"), together with all of Payor's books and records related to the Pledged Assets, all products, proceeds and revenues of the Pledged Assets, and all substitutions for the Pledged Interests and additions to the Pledged Assets, including all stock rights and membership interest rights (including all economic rights, all management and governance rights and all other rights of Payor arising out of Payor's status as a shareholder or member of any affiliated company), rights to subscribe, rights to dividends and distributions of every kind, voting rights, and all other rights and property to which Payor is or may hereafter become entitled on account of the Pledged Assets. The first priority security interest provided hereby is *pari passu* with Note(s) issued by Payor on similar terms as those set forth herein.

[SIGNATURE PAGE FOLLOWS]

**PAYEE**

\_\_\_\_\_

By: \_\_\_\_\_  
\_\_\_\_\_

**PAYOR**

One Stop Systems, Inc.  
a Delaware corporation

By: \_\_\_\_\_  
John W. Morrison, Jr., CFO

**WARRANT TO PURCHASE COMMON STOCK**

**OF ONE STOP SYSTEMS, INC.**

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**WARRANT TO PURCHASE COMMON STOCK  
OF ONE STOP SYSTEMS, INC.**

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This Warrant issued on \_\_\_\_\_, 2019, certifies, for value received \_\_\_\_\_, or registered assigns, is entitled, subject to the terms set forth below, to purchase from One Stop Systems, Inc., a Delaware corporation (“Company”), \_\_\_\_\_ (\_\_\_\_\_) fully paid and non-assessable shares of Common Stock of the Company at the purchase price of \_\_\_\_\_ (\$\_\_\_\_) per share (“Per Share Purchase Price”) at any time or from time to time from the date of this Warrant to and including \_\_\_\_\_, 2024 such price and number of shares being subject to adjustment as provided herein.

**1. Definitions**

As used in this warrant, the following terms, unless the context requires otherwise, have the following meanings:

**1.1 Company.** “Company” includes any corporation that will succeed to or assume the obligations of the Company under this warrant.

**1.2 Common Stock.** “Common Stock,” when used with reference to stock of the Company, means all shares, now or hereafter authorized, of the class of the Common Stock of the Company presently authorized and stock of any other class into which those shares may later be changed.

**1.3 Securities Act.** “Securities Act” means the Securities Act of 1933, or any similar federal statute, and the rules and regulations of the Securities and Exchange Commission (or any other federal agency then administering the Securities Act) under that legislation, all as they may be in effect at the time.

**1.4 Warrant Holder.** The terms “warrant holder,” “holder of warrants,” “holder,” or similar terms when the context refers to a holder of the warrants, mean anyone who at the time is the registered holder of any of the warrants.

**2. Registration Rights**

Notwithstanding any provision of this Warrant to the contrary, each certificate representing any Common Stock issued pursuant to exercise of warrant hereunder will bear the following legend:

THE SECURITIES REPRESENTED HEREBY HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE SECURITIES LAWS OF ANY STATE AND MAY NOT BE SOLD, TRANSFERRED OR OTHERWISE DISPOSED OF EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER SUCH ACT AND APPLICABLE STATE SECURITIES LAWS OR PURSUANT TO AN APPLICABLE EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF SUCH ACT AND SUCH LAWS.

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### 3. Exercise

**3.1 Subscription.** The holder of this Warrant may exercise it in full, or in part, by surrender of this Warrant, with delivery of a Subscription in the form attached hereto as **Exhibit A**, duly executed by the holder, to the Company at its principal office in Escondido, California accompanied by payment in the amount obtained by multiplying the Purchase Price by the number of shares of Common Stock specified on the face of this Warrant.

**3.2 Investor Certificate.** Company may request a written statement that the holder is purchasing the Common Stock or that the transferee is acquiring the Warrant or Common Stock for such holder's or transferee's own account, for investment and not with a view to the sale or distribution of the Warrant or Common Stock nor with any then-present intention of distributing or selling the Warrant or Common Stock. Any such Warrant or Common Stock certificate may, at the Company's option, include any legend considered necessary or desirable to comply with the Securities Act.

**3.3 Partial Exercise.** On partial exercise, the Company will promptly issue and deliver to the holder of this Warrant a new warrant in the name of the Warrant Holder, providing for the right to purchase that number of shares of Common Stock (without giving effect to any adjustment of that number) for which this Warrant has not been exercised.

**3.4 Payment.** Payment may be in cash or by official bank check payable to the order of the Company.

**3.5 Continuing Obligations.** At the time this Warrant is exercised, the Company will, at the holder's request, acknowledge in writing its continuing obligation to afford to that holder any rights to which that holder will continue to be entitled after such exercise in accordance with this Warrant, provided that, if the holder fails to make such request, that failure will not affect the Company's continuing obligation to afford to such holder any such rights.

### 4. Delivery of Stock Certificate

As soon as possible after full or partial exercise of this Warrant, the Company at its expense will cause to be issued in the name of and delivered to the holder of this Warrant, a certificate for the number of fully paid and non-assessable shares of Common Stock to which that holder will be entitled on such exercise, together with any other securities and property to which that holder is entitled on such exercise under the terms of this Warrant. No fractional share will be issued on exercise of rights to purchase under this Warrant. If on any exercise of this Warrant a fraction of a share results, the Company will pay the cash value of that fractional share, calculated on the basis of the exercise price.

## **5. Stock Splits and Combinations**

If the Company at any time subdivides or combines its outstanding shares of Common Stock, this Warrant will, after that subdivision or combination, be evidence of the right to purchase the number of shares of Common Stock that would have been issuable as a result of that change with respect to the shares of Common Stock that were purchasable under this Warrant immediately before that subdivision or combination. If the Company at any time subdivides the outstanding shares of Common Stock, the Purchase Price then in effect immediately before that subdivision will be proportionately decreased, and, if the Company at any time combines the outstanding shares of Common Stock, the Purchase Price then in effect immediately before that combination will be proportionately increased. Any adjustment under this provision will become effective at the close of business on the date the subdivision or combination becomes effective.

## **6. Reclassifications, exchanges and substitutions**

If the Common Stock issuable on exercise of this Warrant is changed into the same or a different number of shares of any other class or classes of stock, whether by capital reorganization, reclassification, or otherwise (other than a subdivision or combination of shares, provided for above), the holder of this Warrant, will on its exercise, be entitled to purchase, in lieu of the Common Stock that that holder would have become entitled to purchase but for such change, a number of shares of such other class or classes of stock equivalent to the number of shares of Common Stock that would have been subject to purchase by the holder on exercise of this Warrant immediately before that change.

## **7. Reorganizations, mergers, consolidations, or sale of assets**

If at any time there is a capital reorganization of the Company's Common Stock (other than a combination, reclassification, exchange, or subdivision of shares provided for elsewhere in this Warrant) or a merger or consolidation of the Company with or into another corporation, or the sale of all or substantially all the Company's properties and assets as, or substantially as, an entirety to another person, then, as a part of such reorganization, merger, consolidation, or sale, lawful provision will be made so that the holder of this Warrant will thereafter be entitled to receive on exercise of this Warrant, during the period specified in this Warrant and on payment of the Purchase Price then in effect, the number of shares of stock or other securities or property of the Company, or of the successor corporation resulting from such merger or consolidation, to which a holder of the Common Stock deliverable on exercise of this Warrant would have been entitled on that event if this Warrant had been exercised immediately before that event. In any such case, appropriate adjustment (as determined by the Company's board of directors) will be made in applying this Warrant to the rights and interests of the holder of this Warrant after the reorganization, merger, consolidation, or sale to the end that this Warrant (including adjustment of the Purchase Price then in effect and number of shares purchasable on exercise of this warrant) will be applicable after that event, as near as reasonably may be, in relation to any shares or other property deliverable after that event on exercise of this Warrant. The Company will, within thirty (30) days after making such adjustment, give written notice (by first-class mail, postage prepaid) to the Warrant Holder.

The notice will set forth, in reasonable detail, the event requiring the adjustment and the method by which the adjustment was calculated and will specify the Purchase Price then in effect after the adjustment and the increased or decreased number of purchasable shares on exercise of this Warrant. When appropriate, advance notice may be given and included as part of the notice required under other provisions of this Warrant.

#### **8. No Impairment**

The Company covenants that it will not, by voluntary action, avoid or seek to avoid the observance or performance of any of the terms of this Warrant, but it will at all times in good faith assist in carrying out all those terms and take all action necessary or appropriate to protect the rights of the holder of this Warrant against impairment.

#### **9. Notice of Adjustments**

The Company will promptly give written notice of each adjustment or readjustment of the Purchase Price or the number of shares of Common Stock or other securities issuable on exercise of this Warrant, by first-class mail, postage prepaid, to the registered holder of this Warrant at that holder's address as shown on the Company's books.

The notice will state the amount of that adjustment or readjustment and show in reasonable detail the facts on which that adjustment or readjustment is based, including a statement of (1) the consideration received or to be received by the Company for any additional shares of Common Stock issued or sold or deemed to have been issued or sold, (2) the number of shares of Common Stock outstanding or deemed to be outstanding, and (3) the Purchase Price in effect immediately before that issue or sale and as adjusted or readjusted because of that issue or sale.

The form of this Warrant need not be changed because of any adjustment in the Purchase Price or in the number of shares of Common Stock purchasable on its exercise. A Warrant issued after any such adjustment on any partial exercise or in replacement may continue to express the same Purchase Price and the same number of shares of Common Stock (appropriately reduced in the case of partial exercise) as are stated on the face of this Warrant as initially issued, and that Purchase Price and number of shares will be considered to have been so changed as of the close of business on the date of adjustment.

#### **10. Miscellaneous**

**10.1 Reservation of Stock.** The Company covenants that it will at all times reserve and keep available, solely for issuance on exercise of this Warrant, all shares of Common Stock or other securities from time to time issuable on exercise of this Warrant.

**10.2 No Rights as a Shareholder.** No holder of this Warrant, as such, will be entitled to vote or receive dividends or be considered a shareholder of the Company for any purpose, nor will anything in this Warrant be construed to confer on any holder of this Warrant, as such, any rights of a shareholder of the Company or any right to vote, to give or withhold consent to corporate action, to receive notice of meetings of shareholders, or to receive dividends or subscription rights or otherwise.

**10.3**      **Modification.** This Warrant and any of its terms may be changed, waived, or terminated only by a written instrument signed by the party against which enforcement of that change, waiver, or termination is sought.

**10.4**      **Governing Law.** This Warrant will be governed by, construed, and enforced in accordance with the laws of the State of California as applied to contracts executed, delivered, and performed solely in that state.

**10.5**      **Expiration.** The right to exercise this Warrant will expire on \_\_\_\_\_, 2024.

In WITNESS WHEREOF, this Warrant is signed on the day and year first above written.

One Stop Systems, Inc., a Delaware corporation

By: \_\_\_\_\_  
Stephen D. Cooper, President and CEO

\_\_\_\_\_

By: \_\_\_\_\_

**EXHIBIT A**  
**SUBSCRIPTION**

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To: One Stop Systems, Inc.

The undersigned, the holder of the attached Warrant, hereby irrevocably elects to exercise the purchase right represented by that Warrant for, and to purchase under that Warrant \_\_\_\_ shares of Common Stock of One Stop Systems, Inc., a Delaware corporation and herewith makes payment of \$\_\_\_\_ for those shares, and requests that the certificates for those shares be issued in the name of, and delivered to \_\_\_\_\_ at the address below.

Date: \_\_\_\_\_

By: \_\_\_\_\_

\_\_\_\_\_ print name

Address:  
\_\_\_\_\_  
\_\_\_\_\_

## SECURITY AGREEMENT

THIS SECURITY AGREEMENT (this "Agreement") is made and entered into effective as of \_\_\_\_\_, \_\_\_\_\_ (the "Effective Date"), by and among (i) ONE STOP SYSTEMS, INC., a Delaware corporation, ("Debtor"), having a mailing address at 2235 Enterprise Street, #101, Escondido, California 92029; (ii) each "Holder" who has executed a counterpart signature page to this Agreement (each, individually, a "Holder" and, collectively, the "Holders"); and (iii) \_\_\_\_\_, an individual, as collateral agent for the Holders (in such capacity, "Secured Party"), having a mailing address at \_\_\_\_\_, with reference to the following facts:

### RECITALS

A. Each of the Holders has advanced a loan (each, individually, a "Loan" and, collectively, the "Loans") to Debtor pursuant to the terms and conditions of a Senior Secured Promissory Note made and given by Debtor to such Holder on or after the date hereof and which recites that the obligations evidenced thereby are secured by this Agreement (each, individually, a "Note" and, collectively, the "Notes").

B. As a condition of extending the Loans evidenced by the Notes, the Holders have required that Debtor grant to Secured Party (for the ratable benefit of the Holders) a security interest in and to the Collateral (as defined herein) pursuant to the terms and conditions of this Agreement.

### AGREEMENT

NOW, THEREFORE, in consideration of the foregoing facts, and upon the mutual covenants and conditions hereinafter contained, the parties hereto hereby agree as follows:

1. **Definitions.**

(a) Unless otherwise defined herein, capitalized terms used in this Agreement shall have the meanings ascribed to such terms by Section 9-102 of the California Uniform Commercial Code (the "UCC") as in effect on the date hereof.

(b) "Obligations" Shall mean and include the following:

(i) any and all indebtedness of Debtor to the Holders incurred under the Notes or incurred under any other documents securing the Notes or otherwise executed or delivered in connection with the Notes (the Notes and this Agreement, together with any such other documents are herein referred to collectively as the "Loan Documents") whether or not any such indebtedness is now existing or hereafter incurred, of every kind and character, direct or indirect, and whether any such indebtedness is from time to time reduced and thereafter increased, or entirely extinguished and thereafter re-incurred, including, without limitation, any sums re-advanced thereunder, or advanced by the Holders for taxes, assessments, insurance and other charges and expenses as hereinafter provided, and all amounts owed under any modifications, renewals or extensions of any of the foregoing obligations;

- (ii) The obligations of Debtor under the terms of any one or more of the Loan Documents;
- (iii) the repayment of (a) any amounts that the Holders may advance or spend for the maintenance or preservation of the Collateral (as defined in Section 2 hereof) and (b) any other expenditures that the Holders may make under the provisions of this any one or more of the Loan Documents or for the benefit of Debtor;
- (iv) all amounts owed under any modifications, renewals or extensions of any of the foregoing obligations; and
- (v) any of the foregoing that arises after the filing of a petition by or against Debtor under the Bankruptcy Code, even if the obligations do not accrue because of the automatic stay under Bankruptcy Code § 362 or otherwise.

(c) “Permitted Liens” means all or any of the following: (i) liens in favor of any or all Holders and/or Secured Party, (ii) liens for taxes or other governmental charges not yet delinquent or being contested in good faith, (iii) liens of carriers, warehousemen, mechanics, materialmen, vendors, and landlords and other similar liens imposed by law incurred in the ordinary course of business for sums not overdue or being contested in good faith, (iv) deposits under workers’ compensation, unemployment insurance and social security laws, and deposits to secure the performance of bids, tenders, contracts or leases, and Liens to secure statutory obligations or surety or appeal bonds or to secure indemnity, performance or other similar bonds in the ordinary course of business, (v) banker’s liens and similar liens (including set-off rights) in respect of bank deposits, (vi) precautionary filings made in connection with any capital lease, and (vii) liens securing purchase money loans and capital leases incurred by Debtor to finance the purchase price of real property, fixtures or equipment.

(d) “Required Holders” means, at any time, the Holders who hold a majority of the aggregate outstanding principal balances of all Notes secured by this Agreement at such time.

## 2. **Grant of Security Interest.**

Debtor, hereby grants to Secured Party (for the ratable benefit of the Holders) a security interest (the “Security Interest”) in the property described on the attached **Exhibit A**, whether now owned or hereafter owned or acquired, and all Proceeds and Products thereof in any form, in all parts, accessories, attachments, special tools, additions and accessions thereto, in all increases or profits received therefrom, and in all substitutions therefor (individually and collectively, “Collateral”). The Security Interest granted by Debtor secures payment of any and all of the Obligations whether or not any such Obligations are now existing or hereafter incurred, of every kind and character, direct or indirect, and whether any such Obligations are from time to time reduced and thereafter increased, or entirely extinguished and thereafter re-incurred, including, without limitation, any sums re-advanced thereunder, or advanced by the Holders for taxes, assessments, insurance and other charges and expenses as hereinafter provided, and all amounts owed under any modifications, renewals or extensions of any of the foregoing obligations.

3. **Perfection of Security Interest.**

(a) Filing of Financing Statement. Debtor hereby authorizes Secured Party, at Debtor's expense, to file in the office of the Delaware Secretary of State initial financing statements, amendments to financing statements and continuation statements, all without Debtor's signature or execution, that cover all Collateral described herein, and all property that becomes Collateral under Section 9315(a)(2) of the UCC. Debtor authorizes Secured Party to perform all other acts which Secured Party deems appropriate to perfect and continue the Security Interest and to protect and preserve the Collateral.

(b) Possession.

- (i) Debtor shall have possession of the Collateral, except where expressly otherwise provided in this Agreement or where Secured Party chooses to perfect its security interest by possession in addition to the filing of a financing statement.
- (ii) Where Collateral is in the possession of a third party, Debtor will join with Secured Party in notifying the third party of Secured Party's security interest and obtaining an acknowledgment from the third party that it is holding the Collateral for the benefit of Secured Party.

4. **Post-Closing Covenants and Rights Concerning the Collateral.**

(a) Inspection. The parties to this Agreement may inspect any Collateral in the other party's possession, upon reasonable notice during normal business hours. In addition, Secured Party shall have the right to verify all or any Collateral in any manner and through any medium Secured Party may consider appropriate and Debtor agrees to furnish all assistance and information and perform any acts which Secured Party may require in connection therewith

(b) Personal Property. The Collateral shall remain personal property at all times. Debtor shall not affix any of the Collateral to any real property in any manner which would change its nature from that of personal property to real property or to a fixture.

(c) Secured Party's Collection Rights. After the occurrence and during the continuance of an Event of Default, Secured Party, at the direction of the Required Holders, shall have the right to enforce Debtor's right against the account debtors and obligors.

(d) Limitations on Obligations Concerning Maintenance of Collateral.

- (i) Risk of Loss. Debtor has the risk of loss of the Collateral.
- (ii) No Collection Obligation. Secured Party shall have no duty to collect any income accruing on the Collateral or to preserve any rights relating to the Collateral.

- (e) No Disposition of Collateral. Secured Party does not authorize, and Debtor agrees not to:
  - (i) make any sales or leases of any of the Collateral, except the sale of Debtor's inventory in Debtor's normal course of business and dispositions of Equipment if replaced with other Equipment of equal or greater value;
  - (ii) license any of the Collateral; or
  - (iii) grant any other security interest in any of the Collateral.

5. **Debtor's Representations and Warranties.**

Debtor warrants and represents that:

(a) Title to and Transfer of Collateral. It has rights in or the power to transfer the Collateral, it is the sole owner of, and has good title to, the Collateral, and its title to the Collateral is free of all adverse claims, liens, security interests or other encumbrances, except the Security Interest, Permitted Liens and other liens incurred in the ordinary course of Debtor's business, and is free from all restrictions on transfer or pledge except as created by this Agreement.

(b) Location of Collateral and Records. All Collateral consisting of Goods is located solely in California. Debtor's records concerning the Collateral are kept at the following addresses: \_\_\_\_\_.

(c) Location, States of Incorporation and, Name of Debtor.

- (i) Debtor's chief executive office is located at 2235 Enterprise Street, Suite 110, Escondido, California 92029.
- (ii) Debtor is a business organization legally created and registered in the State of Delaware; and
- (iii) Debtor's exact legal name is as set forth in the first paragraph of this Security Agreement.

(d) Debtor is authorized to enter into this Security Agreement.

(e) Each Account, Contract Right, Supporting Obligation and Chattel Paper constituting Collateral is genuine and enforceable in accordance with its terms against the party obligated to pay the same.

(f) Each Instrument and each Document of Title constituting Collateral, if any, is genuine and in all respects what it purports to be.

(g) If any Collateral is or will be Investment Property, then such Investment Property is duly and validly authorized and issued, fully paid and nonassessable, is free of all options and charges, and is not subject to any charter, bylaw, statutory, contractual or other restrictions governing its issuance, transfer, ownership or control, except as indicated on the stock certificates for the Investment Property, if any.

(h) If any Collateral is or will be Investment Property, Debtor has delivered to Secured Party all stock certificates or other instruments or documents representing or evidencing the Investment Property, together with corresponding assignments or transfer powers duly executed in blank by Debtor

**6. Debtor's Covenants.**

Until the Obligations are paid in full, Debtor shall:

(a) preserve its existence and not, in one transaction or a series of related transactions, merge into or consolidate with any other entity, or sell all or substantially all of its assets;

(b) not change the state where it is located;

(c) not change its name or its chief executive office address without providing Secured Party thirty (30) days' prior written notice;

(d) will pay all taxes, assessments and other charges of every nature which may be levied or assessed against the Collateral, will insure the Collateral against risks, and in coverage, form and amount, satisfactory to Secured Party, and, at Secured Party's request, will deliver each policy or certificate of insurance therefor to Secured Party;

(e) will defend the Collateral against the claims and demands of all other parties except, as to Inventory, purchasers and lessees in the ordinary course of Debtor's business, will keep the Collateral free from all security interests or other encumbrances, except the Security Interest and Permitted Liens, and Secured Party does not authorize, and Debtor agrees not to sell, transfer, lease, license, or otherwise dispose of any Collateral or any interest therein (except for Permitted Liens) without the prior written consent of Secured Party which consent shall be in Secured Party's sole discretion; except that until the occurrence of an Event of Default as hereinafter provided, Debtor may sell or lease Inventory in the ordinary course of Debtor's business, or dispose of Equipment if replaced with other Equipment of equal or greater value;

(f) will notify Secured Party promptly in writing of any change in the location of any Collateral or of the records with respect thereto, and will permit Secured Party or its agents to inspect the Collateral during normal business hours upon reasonable prior notice;

(g) will keep the Collateral in good condition and repair, and will not use the Collateral in violation of any provisions of this Agreement, of any applicable statute, regulation or ordinance or of any policy insuring the Collateral;

(h) will prevent the Collateral or any part thereof from being or becoming an accession to other goods not covered by this Agreement;

(i) will keep accurate and complete records concerning the Collateral, will mark any and all such records at Secured Party's request to indicate the Security Interest, and, upon Secured Party's request, will upon reasonable notice permit Secured Party or its agents to audit and make extracts from such records or any of Debtor's ledgers, reports, correspondence or other records;

(j) will not create any Chattel Paper without placing a legend on the Chattel Paper acceptable to Secured Party indicating that Secured Party has a security interest in the Chattel Paper;

(k) if an entity, shall maintain its existence as an entity in good standing under the laws of the state of that entity's formation; and

(l) upon demand, will deliver to Secured Party any Documents of Title and any Chattel Paper constituting, representing or relating to the Collateral or any part thereof, if any, any schedules, invoices, shipping documents, delivery receipts, purchase orders, contracts or other documents representing or relating to purchases or other acquisitions, or sales, leases or other disposition of Collateral and Proceeds thereof, and any and all schedules, documents and statements which Secured Party may, from time to time, request.

## 7. **Insurance**

(a) Debtor at all times:

(i) To the extent not insured under the coverage of a commercial property policy issued for real estate owned by Debtor shall keep the Collateral insured under a special form business personal property policy, for the benefit of Secured Party against loss or damage by fire, lightning, windstorm, hail, explosion, collapse and any other perils covered under such special form policy. Such policy shall be in the amount of 100% of the replacement cost for all covered items, adjusted annually to reflect increased value due to inflation, and shall contain an agreed amount endorsement.

(ii) Shall maintain a policy of commercial comprehensive general public liability and property damage insurance. Such policy shall contain a broad form coverage endorsement and shall be on an occurrence basis and not a "claims made" basis, in a minimum amount of \$1,000,000 for each occurrence and \$2,000,000 general aggregate coverage. If such general liability policy covers more than one location, the policy shall contain an endorsement to the effect that the aggregate limit in the policy shall apply separately to each location of Debtor.

(iii) Shall maintain such other insurance and in such amounts as Secured Party from time to time may reasonably request against such other insurable hazards which at the time are commonly insured against for property similar to the Collateral located in or around the region in which the Collateral is located.

(b) All insurance policies required under this Agreement will be written in such manner and with such terms and with such company or companies as shall be approved from time to time by Secured Party. The company providing casualty insurance must be rated at least A, Class V under the most recently published Best's Key Rating Guide, Property & Casualty, must be licensed and admitted to do business in all States where any Collateral is located and must manually sign all policies and endorsements. The business personal property policy shall name Secured Party as loss payee. Without limiting the foregoing, each policy shall provide or have attached a standard non-contributing, non-reporting mortgagee clause satisfactory to Secured Party in favor of and entitling Secured Party, without contribution, to collect any and all proceeds payable under such insurance as its interest may appear; and/or a provision naming Secured Party as an additional insured, whichever is appropriate to the policy in question as determined by Secured Party, and shall also contain a clause providing that such policy may not be canceled, altered, changed, amended or modified, nor shall any coverage therein be reduced, deleted, amended, modified, changed or canceled by either the party named as the insured or the insurance company issuing the policy without at least thirty (30) days prior written notice having first been received by Secured Party. The amount of the deductible under each policy must be acceptable to Secured Party. Each policy must contain language whereby the right of subrogation is waived.

(c) Debtor shall promptly pay when due any and all premiums on all of Debtor's insurance. The policies of such insurance and all renewals thereof are hereby assigned to, and shall be deposited with and held by, Secured Party, as collateral and further security for the Obligations.

(d) In the event of any loss or damage to the Collateral, Debtor shall give notice to Secured Party. Secured Party may make proof of loss thereof if not made promptly by Debtor. Secured Party shall collect and receive the insurance proceeds thereof and endorse drafts of such proceeds, and Secured Party is hereby irrevocably appointed attorney-in-fact of Debtor for such purposes. Debtor hereby authorizes Secured Party, at the option of Secured Party, and without further consent of Debtor to collect, adjust and compromise any losses or claims under any of such insurance, and after deducting costs and expenses of collection (including without limitation, reasonable attorneys' fees and expenses) to apply at Secured Party's option all or part of the proceeds collected by Secured Party (if any) as a credit upon any portion, as selected by Secured Party, of the Obligations, or to repairing, replacing or restoring the Collateral, or both, as the case may be.

8. **Registered Holder of Collateral.**

If any Collateral consists of Investment Property, Debtor authorizes Secured Party to transfer the same or any part thereof into its own name or that of its nominee so that Secured Party or its nominee may appear of record as the sole owner thereof; provided that so long as no Event of Default has occurred as hereinafter provided, Secured Party shall deliver promptly to Debtor all notices, statements or other communications received by it or its nominee as such registered owner, and upon demand and receipt of payment of necessary expenses thereof, shall issue to Debtor or its designee a proxy or proxies to vote and take all action with respect to such Investment Property. After the occurrence of any such Event of Default, Debtor waives all rights to be advised or to receive any notices, statements or communications received by Secured Party or its nominee as such record owner, and agrees that no proxy or proxies issued by Secured Party to Debtor or its designee as aforesaid shall thereafter be effective.

9. **Income from and Interest on Collateral.**

In the event of any Event of Default, Debtor will not demand or receive any income from or interest on the Collateral and if Debtor receives any such income or interest without any demand by it, Debtor will pay the same promptly to Secured Party. Secured Party may apply the net cash receipts from such income or interest to payment of the Obligations on a pari passu basis, provided that Secured Party shall account for and pay over to Debtor any such income or interest remaining after payment in full of the Obligations.

10. **Increases, Profits, Payments or Distributions.**

Whether or not an Event of Default has occurred as hereinafter provided, Debtor authorizes Secured Party: (a) to receive any increase in or profits on the Collateral and to hold the same as part of the Collateral; and (b) to receive any payment or distribution upon redemption, or upon dissolution and liquidation of the issuer, of any Collateral; to surrender such Collateral or any part thereof in exchange therefor; and to hold the net cash receipts from any such payment or distribution as part of the Collateral

11. **Purchase Money Security Interests.**

To the extent Debtor uses the Obligations to purchase Collateral, Debtor's repayment of the Obligations shall apply on a "first-in-first-out" basis so that the portion of the Obligations used to purchase a particular item of Collateral shall be paid in the chronological order Debtor purchased the Collateral.

12. **Events of Default.**

The occurrence of any of the following shall, at the written direction of the Required Holders, be an "Event of Default" hereunder:

(a) Any default or Event of Default (as defined below) by Debtor under the Notes or any one or more of the other Loan Documents or any of the Obligations;

(b) The failure of Debtor to comply with any of the provisions of, or the incorrectness of any representation or warranty contained in, this Agreement, the Notes, or any one or more of the other Loan Documents, or in any of the Obligations;

(c) Transfer or disposition of any of the Collateral, except as expressly permitted by this Agreement;

(d) Attachment, execution or levy on any of the Collateral which is not removed or bonded over within 30 days after Debtor receives notice thereof;

(e) Debtor voluntarily or involuntarily becoming subject to any proceeding under (a) the Bankruptcy Code or (b) any similar remedy under state statutory or common law; or

(f) Debtor shall fail to comply with, or become subject to any administrative or judicial proceeding under any federal, state or local (a) hazardous waste or environmental law, (b) asset forfeiture or similar law which can result in the forfeiture of property, or (c) other law, where noncompliance may have any significant effect on the Collateral.

13. **Default Costs.**

(a) Should an Event of Default occur, Debtor will pay to Secured Party all costs reasonably incurred by Secured Party for the purpose of enforcing its right hereunder, including;

(i) costs of foreclosure;

(ii) costs of obtaining money damages; and

(iii) a reasonable fee for the services of attorneys and other professionals and service providers employed by Secured Party for any purpose related to this Agreement, the other Loan Documents or the Obligations, including consultation, drafting documents, sending notices or instituting, prosecuting or defending litigation or arbitration.

14. **Remedies Upon Default.**

(a) General. Upon any Event of Default, Secured Party (at the written direction of the Required Holders) may pursue any remedy available at law (including those available under the provisions of the UCC), or in equity to collect, enforce or satisfy any Obligations then owing, whether by acceleration or otherwise.

(b) Cumulative Remedies. Upon any Event of Default, Secured Party (at the written direction of the Required Holders) shall have the right to pursue any of the following remedies separately, successively or simultaneously;

- (i) File suit and obtain judgment and, in conjunction with any action, Secured Party may seek any ancillary remedies provided by law, including levy of attachment and garnishment.
- (ii) Take possession of any Collateral if not already in its possession without demand and without legal process. Upon Secured Party's demand, Debtor shall assemble and make the Collateral available to Secured Party as it may direct. Debtor grants to Secured Party the right, for this purpose, to enter into or on any Premises where Collateral may be located.
- (iii) Without taking possession, sell, lease or otherwise dispose of the Collateral at public or private sale in accordance with the UCC.
- (iv) Obtain the appointment of a receiver to handle, maintain, and operate Debtor's Business and apply the net proceeds to the payment of the Obligations, or to sell and dispose of the Collateral under orders of the Court appointing such receiver for the payment thereof.

15. **Foreclosure Procedures.**

(a) No Waiver. No delay or omission by Secured Party to exercise any right or remedy accruing upon any Event of Default shall: (a) impair any right or remedy, (b) waive any default or operate as an acquiescence to the Event of Default, or (c) affect any subsequent default of the same or of a different nature.

(b) Notices. Secured Party shall give Debtor such notice of any private or public sale as may be required by the UCC.

(c) Condition of Collateral. Secured Party has no obligation to clean-up or otherwise prepare the Collateral for sale.

(d) No Obligation to Pursue Others. Secured Party has no obligation to attempt to satisfy the Obligations by collecting them from any other person liable for them and Secured Party may release, modify or waive any Collateral provided by any other person to secure any of the Obligations, all without affecting Secured Party's rights against Debtor. Debtor waives any right it may have to require Secured Party to pursue any third person for any of the Obligations.

(e) Compliance With Other Laws. Secured Party may comply with any applicable state or federal law requirements in connection with a disposition of the Collateral and compliance will not be considered adversely to affect the commercial reasonableness of any sale of the Collateral.

(f) Warranties. Secured Party may sell the Collateral without giving any warranties as to the Collateral. Secured Party may specifically disclaim any warranties of title or the like. This procedure will not be considered adversely to affect the commercial reasonableness of any sale of the Collateral.

(g) Sales on Credit. If Secured Party sells any of the Collateral upon credit, Debtor will be credited only with payments actually made by the Purchaser received by Secured Party and applied to the indebtedness of the Purchaser. In the event the Purchaser fails to pay for the Collateral, Secured Party may resell the Collateral and Debtor shall be credited with the proceeds of the sale.

(h) Purchases by Secured Party. In the event Secured Party purchases any of the Collateral being sold, Secured Party may pay for the Collateral by crediting some or all of the Obligations of Debtor.

(i) No Marshaling. Secured Party has no obligation to marshal any assets in favor of Debtor, or against or in payment of:

- (i) the Notes,
- (ii) any of the Obligations, or
- (iii) any other obligation owed to Secured Party by Debtor or any other person.

16. **Miscellaneous.**

(a) Assignment.

- (i) Binds Assignees. This Agreement shall bind and shall inure to the benefit of the heirs, legatees, executors, administrators, successors and assigns of the Holders and Secured Party and shall bind all persons who become bound as a debtor to this Agreement.
- (ii) No Assignments by Debtor. The Holders and Secured Party do not consent to any assignment by Debtor except as expressly provided in this Agreement and Debtor shall not otherwise assign this Agreement without the prior written consent of the Required Holders.
- (iii) Assignment by Holders. A Holder who assigns its rights under its Note shall also assign its rights and interests under this Security Agreement to the same assignee. If an assignment is made in accordance with the terms of the applicable Note and this Agreement, Debtor and Secured Party shall render performance under this Agreement to such assignee. Each of Debtor and Secured Party waives and will not assert against any such assignee any claims, defenses or set-offs which Debtor or Secured Party could assert against the assigning Holder except defenses which cannot be waived.

(iv) Assignment by Secured Party. Assignments by Secured Party of its rights and obligations under this Agreement shall be governed by Section 17(c) below.

(b) Severability. Should any provision of this Agreement be found to be void, invalid or unenforceable by a court or panel of arbitrators of competent jurisdiction, that finding shall only affect the provisions found to be void, invalid or unenforceable and shall not affect the remaining provisions of this Agreement.

(c) Notices. Any notice, demand request or other communication given in connection with this Agreement shall be deemed sufficient if in writing and sent by registered or certified mail, postage prepaid, return receipt requested, addressed to the party to receive such Notice at its address first set forth above or at such other address as such party may hereafter designate by Notice given in like fashion. Notices shall be deemed given when mailed. Notwithstanding the foregoing, routine communications may be sent by ordinary first-class mail. Any notice given to Secured Party in accordance with this Section 16(c) shall be deemed to have been given simultaneously to all Holders.

(d) Headings. Section headings used this Agreement are for convenience only. They are not a part of this Agreement and shall not be used in construing it.

(e) Governing Law. This Security Agreement and the transaction evidenced hereby shall be governed by, and construed and enforced in accordance with, the laws of the State of California.

(f) Rules of Construction.

(i) No reference to “proceeds” in this Agreement authorizes any sale, transfer, or other disposition of the Collateral by Debtor.

(ii) “Includes” and “including” are not limiting.

(iii) “Or” is not exclusive.

(iv) “All” includes “any” and “any” includes “all.”

(g) Integration. This Agreement is the entire agreement of Debtor, the Holders and Secured Party concerning its subject matter.

(h) Waiver. Any party to this Agreement may waive the enforcement of any provision to the extent the provision is for its benefit.

(i) Additional Security. As further security for payment of the Obligations, Debtor hereby grants to Secured Party a Security Interest in and lien on any and all property and proceeds of Debtor which is or may hereafter be in any Holder’s possession in any capacity, including, without limitation, all monies, escrows and reserves owed or to be owed by any Holder to Debtor. With respect to all of such property, Secured Party shall have the same rights hereunder as it has with respect to the Collateral. Without limiting any other right of Secured Party, whenever

Secured Party (at the written direction of the Required Holders) has the right to declare any Obligations to be immediately due and payable (whether or not it has so declared), Secured Party at its sole election may set off against the Obligations any and all monies then owed to Debtor by the Holders in any capacity, whether or not due, and the Holders shall be deemed to have exercised such right of setoff immediately at the time of such election even though any charge therefor is made or entered on the Holders' and Secured Party's records subsequent thereto.

(j) Right to Perform Duties and Charge Debtor. Upon Debtor's failure to perform any of its duties hereunder, Secured Party may, but shall not be obligated to, perform any or all such duties, and Debtor shall pay an amount equal to the expense thereof to Secured Party forthwith upon written demand by Secured Party.

(k) Right to Collect on Collateral. Secured Party (at the written direction of the Required Holders) may demand, collect and sue on the Collateral (in either Debtor's or Secured Party's name at the latter's option) with the right to enforce, compromise, settle or discharge the Collateral, and may endorse Debtor's name on any and all checks, commercial paper, and any other Instruments pertaining to or constituting the Collateral.

(l) No Waiver. No delay or omission by Secured Party in exercising any right or remedy hereunder or with respect to any Obligations shall operate as a waiver thereof or of any other right or remedy, and no single or partial exercise thereof shall preclude any other or further exercise thereof or the exercise of any other right or remedy. Secured Party may remedy any default by Debtor hereunder or with respect to any Obligations in any reasonable manner without waiving the default remedied and without waiving any other prior or subsequent default by Debtor. All rights and remedies of Secured Party hereunder are cumulative. All duties and obligations of Debtor hereunder are joint and several.

(m) Waivers of Protest and Notice. Secured Party shall have no obligation to take, and Debtor shall have the sole responsibility for taking, any and all steps to preserve rights against any and all prior parties to any Instrument or Chattel Paper, whether Collateral or Proceeds and whether or not in Secured Party's possession. Debtor waives protest of any Instrument constituting Collateral at any time held by Secured Party on which Debtor is in any way liable and waives notice of any other action taken by Secured Party.

(n) Inurement. The rights and benefits of Secured Party hereunder shall, if Secured Party so agrees, inure to any party acquiring any interest in the Obligations or any part thereof. This Security Agreement shall bind all persons who become bound as a debtor to this Security Agreement pursuant to the California Uniform Commercial Code.

(o) Amendments. No modification, rescission, waiver, release or amendment of any provision of this Security Agreement shall be made except by a written agreement signed by Debtor, Secured Party and the Required Holders. Any such modification, rescission, waiver, release or amendment shall be binding upon Debtor, Secured Party and all Holders.

(p) No Effect on Security Interest by Amendment. No extension, alteration or other such modification of the Note or any of the other Loan Documents shall affect the attachment, perfection, validity or priority of this Agreement or the associated financing statements.

(q) Joint and Several Obligations. All obligations of each Debtor hereunder shall be joint and several.

17. **Secured Party and the Holders**

(a) Appointment, Powers and Immunities of Secured Party. Each Holder hereby appoints and authorizes Secured Party to act as its agent hereunder and under the other Loan Documents with such powers as are expressly delegated to Secured Party by the terms of this Agreement, together with such other powers as are reasonably incidental thereto. Secured Party shall not have any duties or responsibilities except those expressly set forth in this Agreement. Secured Party shall not be required or permitted to take any action which is contrary to this Agreement or any other Loan Document or applicable law. Secured Party shall take only such actions with respect to this Agreement and the other Loan Documents as shall be directed by the Required Holders.

(b) Defaults. Secured Party shall not be deemed to have knowledge or notice of the occurrence of any Event of Default hereunder unless Secured Party has received a written notice from a Holder or Debtor, referring to this Agreement, describing such Event of Default and stating that such notice is a "Notice of Default." If Secured Party receives such a notice of the occurrence of an Event of Default, Secured Party shall give prompt notice thereof to all Holders. Secured Party shall take such action with respect to such Event of Default as shall be reasonably directed by the Required Holders. Notwithstanding anything contained in any Loan Document to the contrary, upon the occurrence of an Event of Default, the exercise of any rights and/or remedies set forth in this Agreement or any other Loan Document shall be made only by Secured Party and only at the written direction, or with the written consent, of the Required Holders.

(c) Resignation or Removal of Secured Party. Secured Party may resign at any time by giving ninety (90) days prior written notice thereof to Debtor and the Holders, and Secured Party may be removed at any time with or without cause by the Required Holders upon ninety (90) days prior written notice thereof to Debtor and Secured Party. Upon any such resignation or removal, the Required Holders shall have the right to appoint a successor Secured Party. Upon the acceptance of any appointment as "Secured Party" hereunder by a successor Secured Party, such successor Secured Party shall thereupon succeed to and become vested with all the rights, powers, privileges and duties of the retiring Secured Party, and the retiring Secured Party shall be discharged from the duties and obligations thereafter arising hereunder. If no successor Secured Party is appointed by the Required Holders within ninety (90) days after written notice of Secured Party's resignation or removal, then such resignation or removal shall nonetheless become effective in accordance with such notice and (a) the retiring Secured Party shall be discharged from its duties and obligations under this Agreement and under the other Loan Documents (except that in the case of any Collateral held by Secured Party on behalf of the Holders under any of the Loan Documents, the retiring Secured Party shall continue to hold such Collateral until such time as a successor Secured Party is appointed) and (2) all payments, communications and determinations to be made by, to or through Secured Party shall instead be made by or to each Holder directly, until such time as the Required Holders appoint a successor Secured Party as provided herein.

(d) Secured Party and Collateral. Secured Party shall hold all Collateral for the benefit of the Holders with the intention that each Holder will have an undivided pro-rata interest in all of the Collateral. Any Collateral held by any Holder will likewise be held on behalf of all Holders.

(e) Sharing of Payments

- (i) Each payment of principal and interest received by Secured Party pursuant to this Agreement shall be shared among the Holders pro-rata.
- (ii) Each payment of expenses, charges, costs and fees payable to Secured Party or any Holder pursuant to this Agreement or any other Loan Document shall be shared among Secured Party and/or the Holders that incurred such expense, charge, cost or fee, pro-rata in accordance with (i) the respective amounts so owed to Secured Party and/or such Holders and (ii) the dates on which such amounts became owing to Secured Party and/or such Holders.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the Effective Date.

SECURED PARTY:

\_\_\_\_\_  
\_\_\_\_\_, an individual,  
as collateral agent for the Holders

DEBTOR:

ONE STOP SYSTEMS, INC.,  
a Delaware corporation

By: \_\_\_\_\_  
John Morrison, Chief Financial Officer

**COUNTERPART SIGNATURE PAGE TO  
SECURITY AGREEMENT**

HOLDER:

\_\_\_\_\_  
[Printed Name of Holder]

\_\_\_\_\_  
[Signature]

\_\_\_\_\_  
[Name and Title of Authorized Signatory if  
Holder is an entity]

EXHIBIT "A" to Security Agreement  
Description of Collateral

"Collateral" means all of Debtor's right, title and interest in, to and under the Debtor's assets and equipment, including titles to said assets (the "Pledged Assets"), together with all of Debtor's books and records related to the Pledged Assets, all products, proceeds and revenues of the Pledged Assets, and all substitutions for the Pledged Interests and additions to the Pledged Assets, including all stock rights and membership interest rights (including all economic rights, all management and governance rights and all other rights of Debtor arising out of Debtor's status as a shareholder or member of any affiliated company), rights to subscribe, rights to dividends and distributions of every kind, voting rights, and all other rights and property to which Debtor is or may hereafter become entitled on account of the Pledged Assets. The first priority security interest provided hereby is pari passu with Note(s) issued by Debtor on similar terms as those set forth in the Note.



Certain identified information has been omitted from this document because it is not material and would be competitively harmful if publicly disclosed, and has been marked with "[\*\*\*]" to indicate where omissions have been made.

## ORIGINAL EQUIPMENT MANUFACTURING AND SUPPLY AGREEMENT

This Original Equipment Manufacturing and Supply Agreement (this "Agreement") is made this 1 July 2019 ("Effective Date") by and among Disguise Systems Limited, a company based in the United Kingdom ("Buyer"), Disguise Technologies Limited, a company based in the United Kingdom ("Disguise Tech"), and One Stop Systems, Inc, a Delaware corporation ("Supplier"). In this Agreement, "Party" shall mean Buyer or Disguise Tech or Supplier, and "Parties" shall mean Buyer, Disguise Tech and Supplier. This agreement supersedes and replaces the OEM agreement dated October 1<sup>st</sup> 2015.

### Recitals

A. Supplier has agreed to manufacture and supply certain products as more fully described in this Agreement to Buyer in accordance with the provisions of this Agreement as it pertains to such production-released products. Engineering, Prototype and pre-production products are not covered by the terms of this Agreement.

B. Disguise Tech owns certain intellectual property rights in and to the aforementioned production-released products which Disguise Tech has agreed to grant a license to Supplier for the purpose of Supplier manufacturing and supplying such products to Buyer for the next 5 or more years in accordance with the terms of this Agreement and providing components for replacement and repair for 2 years subsequently after the product is shipped to the Buyer.

C. This Agreement sets forth the terms and conditions of purchases that may occur between the Parties. All such quantities will be specified on Buyer's purchase orders issued under the provisions of this Agreement.

### Agreement

NOW THEREFORE, in consideration of the mutual covenants and agreements herein contained and for other good and valuable consideration, the Parties hereby agree as follows:

#### SECTION A: GENERAL BUSINESS OPERATIONS

##### 1. General Responsibilities of the Parties.

(a) Specifications. Supplier and Buyer agree on a list of specifications (the "Specifications") to which all products currently being produced and all future products that may be produced (the "Product(s)") hereto will be manufactured and supplied in accordance with the terms of this Agreement. Exhibit A hereto may be amended from time to time by mutual written agreement of the Parties.

(b) Certain Responsibilities of Buyer. Buyer will distribute the Products purchased by Buyer from Supplier only in connection with products which Buyer sells, leases and/or licenses, whether directly or indirectly, through sub-tier suppliers and/or distributors or otherwise. Buyer shall be responsible for securing any required U.S. export licenses relating to the Products.

2. **Term of the Agreement.** Subject to the terms of this agreement, the term of this Agreement shall commence on the Effective Date and shall expire on the five (5) year anniversary hereof (the "Term"). Buyer may provide Supplier with written notice, no later than Six (6) months before expiration of the Term that Buyer desires to negotiate with Supplier in good faith for an extension period as Buyer and Supplier may mutually determine of the Term (the "Extension"). If the Parties hereto cannot agree on the terms for such Extension within a period of ninety (90) days following such notice, this Agreement will terminate at the end of the Term.

3) **Exclusive manufacturing Rights**

a) **Geographic area covered.**

- i. Subject to clause (iii) below, Supplier and Buyer agree that Supplier will have exclusive manufacturing rights for all systems sold by Buyer for end shipment into North, Central and South America only.
  - ii. Supplier and Buyer agree that Supplier will have exclusive manufacturing rights for systems sold by Buyer for end shipment into Japan and Korea until such time that the Buyer commences production shipments with a separate manufacturer located on the continent of Asia and, immediately, at such point, this exclusivity right shall automatically terminate.
  - iii. The exclusive manufacturing rights provided in (i) and (ii) above are in effect only while the SG&A (S) and Profit (Z) rates in Exhibit B do not exceed the base rates in Exhibit B factoring in anniversary reductions.
- b) The above right in no way precludes Supplier from selling into other areas of the world if requested by Buyer to do so in accordance with the terms of this Agreement.

4) **Prices: Payment of Invoices.**

(a) The pricing model for all Products ordered after the Effective Date is defined in Exhibit B (the "Price").

(b) The Price provided by the model shall be considered **"not to exceed"** pricing until the next price list is mutually agreed by the Parties and published to the Buyer. The price list shall be published to the Buyer at least every six (6) months, commencing on the Effective Date, or when Products are added or removed from the price list at the request of the Buyer ("Pricing Period").

(c) The Price shall be negotiated and agreed upon at the time the purchase order is placed based on the volumes being ordered. Should the Product specification change at the request or by acceptance by the Buyer, or should the Buyer change quantities on a Purchase Order within the Pricing Period, the Price for the Products may be modified within the Pricing Period, subject to the mutual agreement between the Parties.

(d) Any engineering projects, engineering changes or other non-recurring engineering ("NRE") activities be required by the Buyer on Products that are part of this agreement will be invoiced at the Engineering rate in Exhibit B or as time to time amended and accepted by the Parties. All new Engineering projects for Products that may or may not become part of this Agreement shall be quoted separately to Buyer.

(e) Any cost increases due to sub-tier supplier cost increases shall be transferred to the Buyer at the start of a new Pricing Period or when the next order is placed. The Parties shall act in good faith in agreeing such amended Prices.

(f) Subject to subparagraph (h) below, the parties agree that in respect of any current tariffs in place in respect of supplies purchased by Supplier from China ("China Tariffs") that affect any part of the Products then:

- a. The Supplier shall use best endeavors to take all steps to mitigate the additional material costs resulting (whether directly or indirectly) from the China Tariffs;
- b. The Buyer shall use best endeavors to take all steps to mitigate additional material costs resulting (whether directly or indirectly) from the China Tariffs due to the Buyer's choice of 3<sup>rd</sup> party products required to be purchased by the Supplier. For the avoidance of doubt, if the Supplier identifies a commercially and technically suitable alternative 3<sup>rd</sup> party product that is not subject to China Tariffs and does not significantly change the performance of the Products, the Buyer agrees to best efforts to test and approve the alternate part for production use. If the Buyer unreasonably declines to use the suitable alternative part then the Buyer will be liable for the increased material cost due to the China Tariffs for the life of the Product containing that part;
- c. Except as agreed in Section A clause 4 section (f)(b) above, the Buyer shall only be liable for the China Tariffs (but not including any increased associated costs not already priced in the Pricing model in Exhibit B) for any Purchase Order made between the Effective Date and 31 December 2019;
- d. Except as agreed in Section A clause 4 section (f)(b) above, for Purchase Orders (or proposals) from 1 January 2020 if the Supplier refuses to be liable for all additional costs to the Products that result from the China Tariffs, then the Buyer has the right to immediately terminate the Supplier's (i) exclusivity right contained in Section A clause 3 above and/or (ii) the Minimum Business Commitment contained in Section A clause 4 (l) below.

(g) Subject to subparagraph (h) below, the parties agree that any tariffs or additional costs caused by export or import restrictions, quota or prohibitions are imposed by any government or public authority ("Tariffs") that affect any part of the Products then:

- a. The Supplier shall use best endeavors to take all steps to mitigate the additional material costs resulting (whether directly or indirectly) from the Tariffs;
- b. The Buyer shall only be liable for those Tariffs (but not including any increased associated costs not already priced in the Pricing model in Exhibit B) for any Purchase Order made for 6 months starting with the date that the Tariffs came into force ("6 Month Period");
- c. For Purchase Orders (or proposals) submitted after the 6 Month Period if the Supplier refuses to be liable for all costs in relation to such Tariffs, then the Buyer has the right to immediately terminate the Supplier's (i) exclusivity right contained in Section A clause 3 above and/or (ii) the Minimum Business Commitment contained in Section A clause 4 (l) below.

(h) The Supplier confirms that neither China Tariffs or Tariffs may be retrospectively charged to the Buyer.

(i) All Products purchased will be invoiced by the Supplier to the Buyer upon completion of all work to the configuration on the Purchase Order, including all tests, and delivered to the designated Buyer inventory area the Buyer's location of manufacture currently defined as 2235 Enterprise St, Escondido, CA or 51 Industristrasse, Grobenzel Germany.

(j) Any changes requested by the Buyer to the systems in the Buyer inventory area will incur a 2 production hour minimum charge to change the configuration and re-test the system. New material required for the change will be charged the Price indicated by the pricing model in Exhibit B.

(k) Any material cost reductions after the Effective Date will be applied to the System Price Model 1 year after they are realized ("1 Year Period") and Supplier shall incorporate these savings into the Products with effect from and shall accordingly revise the Price List at either the next 1 January or 1 July whichever date occurs sooner following the 1 Year Period.

(l) If total invoiced Product drops below \$10,000,000 per calendar year, escalating by \$1,000,000 per year on the anniversary of the Effective Date ("Minimum Business Commitment"), then the combined SG&A (S) and Profit (Z) rates in Exhibit B will immediately be fixed at the lower of [\*\*\*] and [\*\*\*] respectively or the prior year's SG&A and Profit Rate for all shipments in the following Quarter until the minimum business level is achieved.

- a. A "Quarter" is defined as a calendar quarter;
- b. The Price shall be adjusted and the Buyer will issue a revised Purchase Order for at the new Price for all Product in subsequent Quarters if any of the following occurs:
  - i. The total of all Invoices minus credit memos for the Product is less than 25% of the Minimum Business Commitment in any two consecutive Quarters.
  - ii. The total of all Invoices minus credit memos for the Product is less than the Minimum Business Commitment in any calendar year.
- c. Minimum business level - If the new Price is adjusted in accordance with paragraph (b) above then as soon as business returns to at least 25% of the Minimum Business Commitment at the next occurring Quarter (meaning that the minimum business level has been satisfied), the Price for all Products shall be immediately adjusted by a revised Purchase Order from the Buyer to the original Price (provided such original amount is lower) for subsequent Quarters.

The Minimum Business Commitment provided in (i) above shall only be in effect while the SG&A (S) and Profit (Z) rates in Exhibit B do not exceed the base rates in Exhibit B factoring in anniversary reductions.

(m) Buyer will pay for Products purchased and accepted by Buyer within [\*\*\*] days after Buyer's receipt of a correct and conforming invoice from Supplier.

(n) Total Credit Line shall be \$[\*\*\*] USD.

(o) The Price does not include shipping charges and sales taxes from the agreed upon FOB Origin / OSS Factory. For the avoidance of doubt, the Price does include shipping charges in respect of the Supplier's supply, manufacturer and assembly prior to the final shipment. Supplier shall arrange for shipping the Products in accordance with Buyer's instructions. Buyer shall prepare all shipping documents and Supplier shall be responsible for printing and incorporating such shipping documents into the Products prior to shipping. Buyer shall pay for such shipping charges; provided that Supplier ships the Products in accordance with Buyer's shipping instructions, otherwise Supplier shall pay

such charges and shall not be entitled to claim such charges from Buyer, nor shall it be entitled to set off such charges against any amounts owed by Supplier to Buyer. Buyer shall pay the aforementioned shipping charges, customs, duties and sales taxes upon Supplier submitting a duly specified invoice to Buyer, provided that Buyer has not submitted satisfactory tax exemption or resale certificates to Supplier, in which case such sales taxes shall not be payable or invoiced by Supplier.

(p) In the event that Supplier owes any payments to Buyer in accordance with this Agreement, Supplier may elect, at its sole discretion, to set off all or part of such amounts against amounts duly owed by Buyer to Supplier either at that time or in the future. Any amounts which may be owing to Buyer by Supplier upon the termination or expiration of the Term of this Agreement (subject to any Extensions) shall become immediately payable.

(q) If Buyer fails to pay Supplier any amounts owed under this Agreement in accordance with its terms then interest will accrue beginning on the due date thereof, at the annual rate of [\*\*\*], however, that in no event will said annual interest rate exceed the maximum legal interest rate for corporations. In the event of any good faith dispute with regard to any due amount, the undisputed portion shall be paid as provided herein. Upon resolution of the disputed portion, any amounts owed to Supplier shall be paid with interest at the rate set forth above, accruing from the date such amounts were originally due. Notwithstanding anything to the contrary stated herein, Supplier may suspend performance of Services and withhold the delivery of any Products or any other materials or deliverables due in connection with the Services until payment in full of all amounts due and owing to Supplier in connection to such Services is delivered to Supplier.

#### 5) **Forecasts, Purchase Orders, Scheduling, and Logistics.**

(a) Buyer and Supplier agree to comply with the provisions set forth in Exhibit C hereto, "Forecasts, Purchase Orders, Scheduling and Logistics."

(c) Purchase Orders entered into by Buyer pursuant to this Agreement shall specify: (i) quantity of Product; and (ii) any other reasonable ordering procedures established or as may be agreed between Buyer and Supplier from time to time.

(d) The agreed period between Buyer's issuance of a Purchase Order and the scheduled delivery date ("Lead-time") is set out in Exhibit C hereto.

(e) All orders shall be governed solely by the terms and conditions of this Agreement. Any terms or conditions contained in either Party's Purchase Orders, invoices, packing lists, or other business forms which are additional to or differ from the provisions of this Agreement, shall have no force or effect whatsoever, unless otherwise expressly agreed in writing between the Parties. A Party's failure to object to any such provisions shall not be deemed a waiver of its rights herein.

6) **Term of Availability.** In consideration for Buyer's purchase of the Products, Supplier grants to Buyer the option to purchase the Products at the last revision Price level agreed between the Parties pursuant to this Agreement, for the period of five (5) years from the date of initial release of each product and subject to availability of any parts. Thereafter, Supplier may, at their discretion, discontinue availability of the Product, provided that, at Buyer's option, Supplier shall first:

(a) Sell Buyer sufficient quantities of the Product as Buyer deems necessary; and

(b) Grant Buyer a royalty-free, non-exclusive, worldwide Manufacturing License (as defined below) such that Buyer may make, have made, sell, modify or otherwise use the Product.

7) **Intellectual Property Rights and Grants of Licenses.**

(a) **Disguise Tech's Intellectual Property Rights.** Supplier agrees and acknowledges that Disguise Tech is the sole and exclusive owner of all rights, title and interest in and to all intellectual property rights, whether now existing or that may exist in the future, including any and all copyrights, patents, design rights (registered or unregistered), trademarks (registered or unregistered), trade names or other intellectual property rights subsisting in respect of the Products or any designs, drawings, prototypes, drafts, plans, representations, models, flow charts, images, illustrations, sketches, plans, models, photographs and documents relating thereto (whether or not stored electronically) and all applicable upgrades and modifications of any of the foregoing, with the exception of the OSS IP Rights, as defined below ("Disguise Tech IP Rights").

(b) **OSS's Intellectual Property Rights.** Supplier is the sole and exclusive owner of all rights, title and interest in and to all intellectual property rights, whether now existing or that may exist in the future, including any and all copyrights, patents, design rights (registered or unregistered), trademarks (registered or unregistered), trade names or other intellectual property rights subsisting in respect of the Products or any designs, drawings, prototypes, drafts, plans, representations, models, flow charts, images, illustrations, sketches, plans, models, photographs and documents relating thereto (whether or not stored electronically) of the elements of the Product which have been developed, designed by Supplier and implemented as part of the Products as described in Exhibit F hereto ("OSS IP Rights").

(c) Disguise Tech hereby grants to Supplier a non-exclusive license of the Disguise Tech IP Rights for the Term of this Agreement and any Extensions ("**License Period**") for the territory of the world (the "**Territory**") for the sole purpose of manufacturing the Products in accordance with the terms and conditions of this Agreement (the "**License**"). Disguise Tech hereby acknowledges and declares that the consideration that it receives through Buyer's purchase of the Products for the Prices pursuant to this Agreement constitutes the full, global and definitive consideration for the granting of the License to Supplier.

(d) Supplier hereby assigns to Disguise Tech, on an exclusive basis, throughout the world, in perpetuity (or at least for the legal duration of all intellectual property rights and their renewals, including, but not limited to, copyright) and for all purposes, all of the OSS IP Rights, which assignment shall become effective upon the expiry of the Term of this Agreement (including any Extensions or Revisions) or any earlier termination of this Agreement in accordance with its terms and conditions. Supplier hereby acknowledges and declares that the consideration which it receives through the sale of the Products to Buyer during the Term (and any Extensions) in accordance with this Agreement constitutes the full, global and definitive consideration for the assignment of the OSS IP Rights to Disguise Tech hereunder. Assignment of IP Rights does not include Manufacturing Rights unless exercised under Section A.8 below.

8) **Manufacturing Rights.**

(a) The Supplier agrees to provide the Buyer with the most recent copy of the Product manual, block diagrams and viewable mechanical model files (i.e. eDrawing) format for use as first level support documentation and Product data sheets, upon Buyer's request.

(b) Further design and manufacturing files will be made available to the Buyer as part of this Agreement in the following manner:

(c) In the event that Buyer decides to have any of the Products manufactured internally or by a third party after the relevant Product(s) has been designed and prototypes manufactured and delivered to Buyer, during the Term of this Agreement and Extension, then Buyer shall inform Supplier in writing of its decision to do so ("Alternative Manufacturing Notice") at least six months in advance (or such other period as agreed between the parties), and Buyer and Supplier shall thereafter enter into a manufacturing license agreement ("Manufacturing License Agreement") which shall include, without limitation, the following terms and conditions:

(i) Supplier shall grant to Buyer all licenses and rights necessary for Buyer to manufacture the Products or to grant the same rights to a third party to manufacture the Products in consideration for the following applicable fees :

a. A one-time license fee of [\*\*\*], paid upon receipt including any applicable taxes for each "System" Product, if the Buyer provides Supplier with an Alternative Manufacturing Notice within twenty-four (24) months of the first Production Shipment of the relevant Product to the Buyer; or

b. A one-time license fee of [\*\*\*], paid upon receipt including any applicable taxes for each "System" Product, if the Buyer provides Supplier with an Alternative Manufacturing Notice between twenty-four (24) months and forty-eight (48) months of the first Production Shipment of the relevant Product to the Buyer; or

c. A one-time license fee of [\*\*\*], paid upon receipt including any applicable taxes for each "System" Product, if the Buyer provides Supplier with an Alternative Manufacturing Notice more than forty-eight (48) months of the first Production Shipment of the relevant Product to the Buyer;

d. A one-time fee of [\*\*\*] paid upon receipt, including any applicable taxes for each "System" Product, if the Buyer has exercised its right to terminate this agreement in accordance with Section C.5.(a) (*Termination for Cause*)

e. The first Production Shipment date of a product is defined as the first unit shipment of a System Product from a Purchase Order that contains (i) the production system part number and (ii) is not otherwise labeled as a prototype unit in the referenced Supplier quote or (iii) a date by other mutual agreement of the Buyer and Seller.

(ii) Supplier shall provide and deliver to Buyer copies of the most recent bill of materials and drawings for all parts designed on behalf of the Buyer. Drawings do not include common off the shelf items from third parties or items not designed on behalf of the purchaser.

(d) On or subsequent to first production shipment of the Products to Buyer and at Buyer's written request for future Product revisions, Supplier shall deposit with an escrow agent, pursuant to an executed escrow agreement, a copy of the Manufacturing Documentation, all for the purpose of allowing Buyer to exercise its Manufacturing License. Escrow fees will be the responsibility of the Buyer.

## **SECTION B. PRODUCT QUALITY**

### **1. Product Warranties.**

(a) Supplier warrants that it has the right to manufacture and convey the Product and that each Product will be free from all liens and encumbrances (including free from any claim that such Product infringes any third party's intellectual property rights), defects in material, workmanship and design and will function in accordance with and will conform to the Specifications for a period of [\*\*\*] from shipment of such Product manufactured at Suppliers authorized facilities to the Buyer ("Warranty Period"). The warranty period can be extended to up of [\*\*\*], prior to the expiration of the original warranty.

(b) Buyer or Buyer's customer shall ship the purported non-conforming Product to the Supplier authorized repair facilities as listed in Appendix E at the Buyer's expense. Purported non-conforming product shipped to any other authorized or non-authorized repair facility is the sole responsibility of the Buyer. Supplier shall inspect and verify if the Product is non-conforming and either replace or repair (as Supplier may determine at its discretion) any Products which do not perform in accordance with the Specifications during the Warranty Period. Supplier shall complete such repair or replacement and ship such repaired or replacement Products to Buyer or to Buyer's customer at Supplier's cost (for shipping) within [\*\*\*] of Supplier's receipt of such Products at its facility. Such replacement or repaired Products shall be covered by the warranty set forth in subsection (a) above for the longer of (i) ninety (90) days from shipment of the replacement Product and (ii) the remaining portion of the original Warranty Period. Further, the parties may agree to replace parts in accordance with Exhibit E.

(c) Supplier's additional warranty terms can be found at [www.onestopsystems.com](http://www.onestopsystems.com) and are incorporated into this agreement in its entirety and as updated from time to time insofar as they do not limit the scope of the warranties contained in this Agreement . EXCEPT FOR THE WARRANTIES SPECIFIED IN THIS AGREEMENT, SUPPLIER DOES NOT MAKE AND EXPRESSLY DISCLAIMS ALL OTHER WARRANTIES, WHETHER EXPRESS OR IMPLIED, INCLUDING, WITHOUT LIMITATION, THE IMPLIED WARRANTIES OF MERCHANTABILITY , FITNESS FOR A PARTICULAR PURPOSE.

## **2. Inspection and Acceptance.**

(a) Supplier shall inspect all Products before shipment to ensure conformance with the Supplier's applicable warranty provisions. In the event that Supplier's conformance level falls below [\*\*\*] due to issues for which Supplier is responsible, for Products delivered during any consecutive three (3) month period, as measured by taking all failures over the last 90 days on all products shipped in the last 90 days. Supplier will provide a corrective action plan within ten (10) business days of Buyer notifying Supplier of such non-conformance. If the Supplier's corrective action plan does not improve Supplier's conformance level to [\*\*\*] or better during the next 90 days following the implementation of the Supplier's corrective action plan, Supplier shall be deemed to be in material breach of this Agreement in accordance with Section C clause 5 of this Agreement and the provisions of Section C clause 5 shall apply. Without prejudice to the forgoing, if the Supplier's corrective action plan does not improve Supplier's conformance level to [\*\*\*] or better during the next 90 days following the implementation of the Supplier's corrective action plan, Buyer may adjust the deliveries of existing orders until Supplier once again achieves a [\*\*\*] conformance level for a consecutive 90 day period.

(b) Buyer reserves the right to inspect the Products being supplied by Supplier to ensure that they meet the Specifications. Buyer shall have twenty-eight (28) days from receipt of Products to perform such inspection. Buyer may return Products which fail to meet the Specifications by first contacting the Supplier for a valid Return Materials Authorization ("RMA") number that shall appear on any and all paperwork, packing lists, air-bills, etc. pertaining to such shipment returned to Supplier. Supplier reserves the right to reject any shipment of returned Product that does not contain a valid RMA number. Supplier shall either repair or replace (at Supplier's discretion) any such Products returned to Supplier and Supplier shall return such repaired or replacement Product to Buyer or to Buyer's customer at Supplier's cost (for shipping) within [\*\*\*] of Supplier's receipt of such Products at its facility.

(c) Supplier shall provide, within [\*\*\*] of Buyer's request and in a mutually agreed upon format, the failure analysis and closed loop corrective action for each Product or group of Products with identical failures and corrective actions. The Supplier shall reserve the right to charge the Buyer a minimum of one (1) production hour per Product that is returned for repair and for which the failure analysis is "No Fault Found" ("NFF"). It is the intent of the Supplier to work with the Buyer to fashion a minimum test suite to be used by the Buyer before returning product to minimize NFF reports.

## **SECTION C. OTHER MATTERS**

### **1. Non-Disclosure.**

(a) Each Party hereto acknowledges that the transactions contemplated by this Agreement will require an exchange of confidential information, including, without limitation trade secrets, proprietary technological and other commercially sensitive information, customer lists and similar information which is of a confidential or proprietary nature (collectively, "Confidential Information"). With respect to such Confidential Information Supplier and Buyer agree as follows.

(b) Each Party shall hold in confidence all Confidential Information of the disclosing Party and shall not disclose to any other person or use such Confidential Information for any purpose other than to as necessary under this Agreement.

(c) The obligations of subsection (b) above shall not apply to information which is proved using tangible evidence to:

- (i) be or have become available to the public from a source other than the receiving Party;
- (ii) be or have been released in writing by the disclosing Party as being no longer Confidential Information which is subject to this Agreement;
- (iii) be or have been lawfully obtained by the receiving Party from a third party not subject to any nondisclosure obligation;
- (iv) have become lawfully known to the receiving Party prior to such disclosure; or
- (v) Have been developed by the receiving Party completely independently of the disclosing Party's Confidential Information.

(d) Each Party acknowledges that a violation of this Section C.1. Would constitute irreparable damage to the disclosing Party and that any remedy at law would be inadequate and thereby consents to the entry of injunctive relief against such violation without the requirement of posting a bond.

(e) The Parties acknowledge that the receiving Party shall obtain no rights of any kind in connection with the other Party's Confidential Information and that any additional know-how, process, or improvements based upon the Confidential Information of the other Party shall be subject to ownership and other rights of the other Party, except as may otherwise be provided in this Agreement.

(f) Upon the written request of the disclosing Party, the receiving Party shall promptly return or certify the destruction of the disclosing Party's Confidential Information, (unless such Confidential Information is necessary for performance of this Agreement).

**2. Trademarks.** Each Party hereby grants to the other Party all necessary permissions for the other Party to utilize the trademarks ("Marks") owned by the granting Party as expressly instructed by the Mark owner, solely in relation to the manufacture and marketing of the Products. Nothing in this Agreement will create in the Buyer or Supplier any rights in the Marks of the other party.

**3. U.S. Customs, Marking and Duty Drawback Requirements.**

(a) Country of Origin.

(i) Supplier shall mark each Product with the "Country of Origin" (manufacture), in compliance with Section 304 of the United States Tariff Act (or any successor act). The Product must be conspicuously marked with the Country of Origin.

(ii) For each delivery against purchases made under this Agreement, Supplier shall furnish Buyer, at Buyer's request, with a signed certificate stating Country of Origin (manufacture) by quantity and Supplier's part number.

(b) Commercial Invoices. Buyer shall provide a Commercial Invoice with each shipment made against any order placed by Buyer. The Commercial Invoice shall be used for U.S. Customs clearance. The Commercial Invoice shall be in English and contain the following information: name and address of manufacturer/Supplier (where the manufacturer is, not the Supplier); Country of Origin (manufacture) of the Product; name and address of Buyer; the quantity and unit price; the type of currency involved; the purchase price in the currency of the purchase; the terms of sale (i.e., FOB Escondido, CA); freight charges; Supplier's part number; Buyer's contact name; and Buyer's purchase order number.

4. **Similar Products.** Supplier acknowledges that Buyer (both itself and through its engagement of third parties) designs, develops and acquires hardware and software products both as stand-alone soft-ware and hardware products and for use with its own products and that existing or planned hardware and software independently developed or acquired by Buyer (or its third party contractors) may contain ideas, designs, features, specifications, uses and concepts similar to those contained in the Products. Supplier agrees that entering this Agreement shall not preclude Buyer in any way from using such ideas, designs, features, specifications, uses and concepts to develop or acquire similar hardware and software for any purpose without obligation to the Supplier, provided Buyer does not intentionally or knowingly infringe the OSS IP Rights, subject to the provisions of Sections A.7 and A.8.

5. **Termination for Cause.**

(a) Either Party may terminate this Agreement on thirty (30) days prior written notice to the other Party in the event the other Party materially breaches any of its obligations under this Agreement. For purposes of the foregoing a material breach shall include, without limitation, the following:

(i) Supplier fails to deliver Products on time or in sufficient quantities in accordance with Buyer's order and fails to remedy such failure within fifteen (15) days of Buyer notifying Supplier of such failure, except if such non-delivery of Products is related to any non-payment by Buyer of fees due to Supplier under this Agreement.

(ii) Products delivered by Supplier fail to conform to the Specifications in Products in accordance with Buyer's order and fails to remedy such failure within fifteen (15) days of Buyer notifying Supplier of such failure.

(iii) Either Party fails to perform or breaches any other material obligation under this Agreement and where such failure is capable of remedy, fails to remedy such failure or breach within fifteen (15) days of the other Party notifying the Party in breach.

(iv) Any representation or warranty of either Party shall have been found to be false or misleading.

(v) either party files a petition in bankruptcy, has a petition filed against it regarding bankruptcy, is adjudicated bankrupt, or makes any assignment for the benefit of creditors that has a material adverse effect on that party's ability to perform its obligations under this Agreement, including, without limitation, payment obligations.

(b) Buyer's sole liability to Supplier for such termination (when Buyer is at fault as per Section C.5.(a) above) shall be to pay Supplier any unpaid balance due for conforming Product delivered against Buyer's Purchase Order(s), and material purchased and pipelined to fulfill open purchase orders before receipt of Buyer's termination notice.

6. **Indemnification .**

(a) Supplier hereby covenants and agrees to indemnify, defend and hold harmless Buyer including its affiliates, officers, directors and employees, free and clear and harmless from, and against, any and all claims, administration of claims, demands, losses, causes of action, liabilities, costs and expenses (including reasonable attorneys' fees) caused by, resulting from or in any way connected with (a) Supplier's acts (including but not limited to any breach of any third party intellectual property rights), omissions or negligence, or the acts, omissions or negligence of Supplier's employees, agents, contractors or permitted assignees and (b) Supplier's breach of this Agreement or any of their representations or warranties contained in this Agreement.

(b) Buyer hereby covenants and agrees to indemnify, defend and hold harmless Supplier including its affiliates, officers, directors and employees, free and clear and harmless from, and against, any and all claims, administration of claims, demands, losses, causes of action, liabilities, costs and expenses (including reasonable attorneys' fees) caused by, resulting from or in any way connected with (a) Buyer's acts, omissions or negligence, or the acts, omissions or negligence of Buyer's employees, agents, contractors or permitted assignees and (b) Buyer's breach of this Agreement or any of their representations or warranties contained in this Agreement..

(c) Buyer or Supplier ("Claimant") shall notify the other Party ("the Defendant") promptly in writing of the existence of any such claim, demand or suit, which if sustained, would give rise to liability on the part of that Party. The Defendant shall have the option to designate counsel to defend such claim, demand or suit and it is understood that Defendant shall be responsible for the fees of such counsel designated by it and control such defense. The Claimant shall cooperate in the defense of any such claim, demand or suit and may participate in the defense of any such claim, demand or suit with counsel of its own choosing (if the Claimant does not approve counsel designated by the Defendant) at its own expense, it being understood that the Defendant shall not be responsible for the payment of any fees of any such counsel. The Claimant shall not take any action to compromise or settle any such claim, demand or suit unless consented to in writing by the Defendant.

**7. Limitation of Liability.** IN NO EVENT WILL EITHER PARTY BE LIABLE TO THE OTHER PARTY UNDER THIS AGREEMENT FOR ANY SPECIAL, INCIDENTAL, INDIRECT, PUNITIVE OR CONSEQUENTIAL DAMAGES (INCLUDING LOST PROFITS AND LOST BUSINESS), WHETHER BASED ON BREACH OF CONTRACT, TORT (INCLUDING NEGLIGENCE), PRODUCT LIABILITY, FUNDAMENTAL BREACH, OR OTHERWISE ARISING OUT OR RELATED TO THIS AGREEMENT, AND WHETHER OR NOT SUPPLIER HAS BEEN ADVISED OF THE POSSIBILITY OF SUCH DAMAGE. NOTWITHSTANDING ANYTHING ELSE TO THE CONTRARY IN THIS AGREEMENT, THE MAXIMUM LIABILITY OF:

a. SUPPLIER UNDER THIS AGREEMENT WILL NOT EXCEED THE HIGHER OF: (i) AGGREGATE AMOUNT OF PAYMENTS RECEIVED BY SUPPLIER UNDER THIS AGREEMENT IN THE TWELVE (12) MONTH PERIOD PRECEDING THE DATE OF THE CLAIM IN QUESTION; AND (ii) US\$5MILLION; AND

b. BUYER UNDER THIS AGREEMENT WILL NOT EXCEED £5MILLION.

**8. Survival.** In the event of any termination of the entire Agreement, (a) the provisions of Sections A.4, A.5, A.6, A.7, A.8, B.1, C.1, C.2., C.4, C.5, C.6, C.7, C.8, and D shall survive the termination or expiration of this Agreement and shall bind the Parties and their legal representatives, successors, and assigns, and (b) the rights of end-user customers of Buyer under any licenses of Products granted during the term of this Agreement shall survive.

**9. Insurance.** Supplier shall procure and maintain in full force and effect at all times comprehensive insurance policies covering all of Supplier's obligations under this Agreement, including, without limitation, general liability insurance and product liability insurance in the amount of [\*\*\*] in any one occurrence and insurance against perils, including but not limited to, fire, freezing, lightning, explosion, riot, civil commotion, smoke or sinkhole, in the amount of [\*\*\*] in any one occurrence.

**10. Risk Management and Liability Release.**

(a) The Supplier shall maintain a Business Resumption Plan for any event, such as natural or man-made disasters, that impact Supplier's ability to deliver Products for a prolonged period of time.

(b) The Supplier shall conform to all local, state, and federal laws, rules, and regulations in performing its obligations under this Agreement.

**SECTION D. MISCELLANEOUS PROVISIONS**

1. **Publicity.** Unless required by law, any announcements or similar publicity with respect to this Agreement or the transactions contemplated herein shall be only at such time and in such manner and shall consist of such contents as both Parties shall mutually agree to in writing.
2. **Independent Parties.** Supplier and Buyer agree that their relationship is not that of joint venture, principal and agent, or franchiser and franchisee. Supplier and Buyer are independent contractors acting for their own accounts and neither is authorized to make any commitment or representation, express or implied, on the other's behalf unless authorized in writing.
3. **Assignments.** Neither Party may assign this Agreement nor any of the rights or obligations hereunder voluntarily or by operation of law without mutual agreement, which shall not be unreasonably withheld.
4. **No Waiver.** The waiver by either Party of any breach of this Agreement by the other Party in a particular instance must be in a signed writing referring expressly to this Agreement and shall not operate as a waiver of subsequent breaches of the same or a different kind. Either Party's exercise or failure to exercise any rights under this Agreement in a particular instance shall not operate as a waiver of said Party's right to exercise the same or different rights in subsequent instances.
5. **Headings.** The section headings contained herein are for convenience only and are not intended to affect the meaning or interpretation of this Agreement.
6. **Notices.** All notices and demands of any kind, that either Supplier or Buyer may be required or desire to serve upon the other Party under this Agreement, shall be in writing and shall be served by personal delivery, confirmed facsimile, nationally recognized courier or U.S. first class mail, return receipt requested, at the following respective addresses:

Supplier:

One Stop Systems, Inc.  
2235 Enterprise St, #110  
Escondido, CA 92029  
Attn: Steve Cooper

Buyer:

Disguise Systems Limited  
[\*\*\*]  
[\*\*\*]  
Attn: [\*\*\*]

If by personal delivery or courier, service shall be deemed complete upon such delivery. If by mail, service shall be deemed complete upon the expiration of the fourth day after the date of mailing. The above addresses may be changed at any time by giving ten (10) days prior written notice.

7. **Force majeure.** Neither Party shall be responsible for failure to perform herein for a period of not more than one hundred and eighty (180) consecutive days due to causes beyond its reasonable control, including, but not limited to government regulations, work stoppage, fires, civil disobedience, embargo, war, riots, rebellions, earthquakes, strikes, floods, water and the elements.
8. **Severability.** In case any one or more of the provisions contained herein shall, for any reason, be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision of this Agreement, but this Agreement shall be construed as if such invalid, illegal or unenforceable provisions had never been contained herein unless the deletion of such provision or provisions would result in such a material change as to cause completion of the transactions contemplated herein to be unreasonable.

9. **Entire Agreement.** This Agreement, together with any other documents and Exhibits incorporated herein by reference, constitutes the entire agreement between the Parties hereto pertaining to the subject matter hereof. Any and all written or oral agreements heretofore existing between the Parties pertaining to the subject matter of this Agreement are expressly canceled except to the extent any rights, remedies, obligations or liabilities of the parties that have accrued up to the date of this agreement including the right to claim damages in respect of any breach of any agreement which existed at or before the date of this agreement. The provisions of this Agreement shall supersede any contravening or inconsistent terms of any purchase order, invoice, packing slip, bill of lading or other commercial form issued by Buyer or Supplier in connection with the Product.

10. **Counterparts.** This Agreement may be executed in two or more counterparts. All such counterparts will constitute one and the same agreement.

11. **Modifications** Any modification of this Agreement must be in writing and signed by the Party to be charged.

12. **Governing Law** This Agreement shall be governed by and construed in accordance with the laws of the State of California without regard to conflict of laws rules which would cause the laws of any other jurisdiction to apply.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK; SIGNATURE PAGE FOLLOWS.]

IN WITNESS WHEREOF, the Parties hereto have executed this Agreement by their respective duly authorized representatives as of the Effective Date.

ONE STOP SYSTEMS, INC.

Disguise Systems Limited.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

Disguise Technologies Limited

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

**EXHIBIT A**  
**PRODUCT AND SPECIFICATIONS**

Any and all systems and parts on the current agreed upon price sheet (see exhibit B)

**EXHIBIT B****PRICE**

- The Pricing for all forecasted items will be determined by the use of the pricing model (see below).
- Purchase Orders will be placed using the Prices from the current Price List.
- [\*\*\*].
- [\*\*\*].
- The Supplier may use different SG&A and/or Profit Rates for System Products in the Price List but if these rates are above the base rates in this section (as adjusted for the agreed percentage point reductions), the Exclusive Manufacturing Rights and the Minimum Business Commitments shall automatically no longer apply.
- Purchase Orders in place prior to a new Pricing Period will not be repriced.
- Purchase Orders in place prior to the Effective Date will not be repriced.
- The gross amounts that SG&A and/or Profit Rates percentages are measured against shall not include sales taxes or any other similar type of taxes.
- All other pricing based on quantity discounts beyond the[\*\*\*] pieces is valid only for Purchase Orders placed by the Buyer to the Supplier on the same day for scheduled delivery over the immediate 12 month period following the date of the Purchase Order unless agreed otherwise by mutual agreement of both Parties.
- The price list can be updated between Pricing Periods to reflect a new volume of an expected order or if a new product is introduced between Pricing Products.
- From time to time Buyer may ask the Supplier for material to be pipelined to cover longer lead time needs. Any goods purchased on behalf of Buyer at their request will be Buyers liability. If the program is terminated, or the material is not used within one (1) year of receipt of the pipelined items, Supplier may invoice the Buyer for the material. Buyer shall not be liable for surplus material if Supplier failed to use the pipelined material in respect of purchase orders during that time.
- Material cost is calculated as the average cost for items in stock and may not entirely reflect the last price paid for an item.
- All components of the pricing model will be reviewed every Pricing Period to determine the new pricing model and Price List for the next Pricing Period.
- The production labor rate (Y) is set at the Effective Date
  - Production labor is defined as production activities including, but not limited to, pull, kit, build, test, and any special request performed by Supplier production employees. This is a burdened labor rate for production employees (Direct Labor) without SG&A. The production labor rate will be reviewed and adjusted every six months
  - Buyer and Supplier will work together in good faith to reduce labor hours to lower future costs
- The engineering labor rate is set at the Effective Date
  - Engineering labor for current sustaining engineering required for Products will be charged at the above rate.
  - Engineering of new products that may or may not become part of this agreement will quoted separately and not part of this agreement.
- Pricing model  
[\*\*\*]

\* This figure shall be subject to the percentage point reductions as fully described above

- Based on the Price List in this section and the minimum business level without incurring Price adjustments of ten million (\$10,000,000) USD per year, escalating by one million (\$1,000,000) per year over the 5 year term of this agreement the approximate expected value of this agreement is sixty million (\$60,000,000) USD. The approximate expected value and term of the agreement does not guarantee current or future business that will be transacted under this agreement between the Buyer and the Supplier. Further, for the avoidance of doubt, the Buyer shall not be liable to the Supplier or any other party for any loss or damages or any other remedy pursuant to this agreement which is measured by way of reference to this proposed valuation. The Buyer shall place all purchase orders and exercise all options under this agreement per the terms outlined herein.

[\*\*\*]

**EXHIBIT C**

**FORECASTS, PURCHASE ORDERS, SCHEDULING, and LOGISTICS**

1. Forecasts. Buyer shall provide a minimum of a 6 month rolling forecast by the end of each month. Such forecasts shall not be binding on Buyer. Supplier will procure, manufacture and ship pursuant to Purchase Orders issued by Buyer for the quantity of Products within the parameters set forth in the 6 month forecasts and rolling outlooks. Supplier shall ship Products to such locations and in such manner and quantities as Buyer shall direct.
2. Lead-times. Minimum Lead-times for the Product shall be [\*\*\*] after receipt of Purchase Order. Buyer will request [\*\*\*] before the start of a month what items they will be pulling from their Purchase Order (also known as "Call Down"), for production-released products. This will come in the form of an email stating all quantities and part numbers that Supplier will be expected to fulfill from the current open purchase orders.
3. Purchase Orders. Buyer and Supplier agree on the following:
  - [\*\*\*] minimum purchase order release (aka, Call Down)
  - Buyer is liable for all materials the Supplier is committed to via their purchase orders to their vendors or for items in stock to meet customers placed purchase orders. This liability will never exceed the amounts on open purchase orders.
4. Rescheduling. Buyer and Supplier shall agree to the following rescheduling guidelines of approved and scheduled forecasts:
  - [\*\*\*]
  - [\*\*\*]
  - [\*\*\*]
  - [\*\*\*]
5. Billing / Title Transfer. Buyer and Supplier agree to the following Billing and Title Transfer of products and services provided by Supplier:
  - Incoterms: FOB, origin
  - [\*\*\*]
  - [\*\*\*]

**EXHIBIT D**

**SUPPLIER CHANGES TO PRODUCT**

1. Supplier agrees to provide Buyer's designate development contact person with a written change notification ("Engineering Change Order" or "ECO") of any changes to any designs, specifications or other documents or tooling relating to the Product within [\*\*\*] of Supplier's decision to implement any proposed change. Such notification will clearly state the reason for the change and the related cost of implementing the change.
2. If Buyer determines that any change may affect form, fit or function of the Product, Buyer will give Supplier written notice to such effect within [\*\*\*] of Buyer's receipt of Supplier's notification of change. The parties shall use reasonable endeavors to agree any proposed changes to the Product but no changes to the Product will be implemented without mutual agreement of both Parties.
3. Buyer may purchase Product for evaluation and verification purposes once the change has been implemented.

**EXHIBIT E**

**APPROVED REPAIRS IN THE FIELD**

List of parts that may be changed by Buyer and Buyer's customer outside of an Authorized Service Center without voiding the Product Warranty. The current approved repairs include

1. [\*\*\*]
2. [\*\*\*]
3. [\*\*\*]

**Authorized service centers for the Products:**

- OSS HQ: 2235 Enterprise St, Suite 110, Escondido CA USA 92029
- OSS GmbH (Bressner): Industriestraße 51, D - 82194 Gröbenzell, Germany
- Disguise HQ: [\*\*\*]

**EXHIBIT F**

**OSS IP RIGHTS – PRODUCT ELEMENTS**  
as per Section A.7.(b)

Elements which are existing or have been developed, designed, adapted, modified or otherwise devised by Supplier for the purpose of being incorporated in, added to or otherwise forming part of one or more of the products for Buyer.

General Description:

- Formal and informal design, updates and re-design of the products
- Improvements to the manufacturing, testing, logistics and assembly of the products
- [\*\*\*] design based on prior OSS product IP designs
- All design and production considerations including but not limited to:

- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]
- [\*\*\*]

For the avoidance of doubt, all the products' specifications actually supplied in writing to Supplier by the Buyer are owned and provided by Disguise Tech to the Supplier and are not included in the OSS IP Rights. All specifications of the Product derived as a result of the Supplier design and execution on the Disguise Tech written specifications are included in the OSS IP Rights.

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO  
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Steve Cooper, certify that:

1. I have reviewed this quarterly report on Form 10-Q of One Stop Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) [paragraph omitted in accordance with Exchange Act Rule 13a-14(a)];
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 8, 2019

By: /s/ Steve Cooper

**Steve Cooper**  
**President and Chief Executive Officer**  
**(Principal Executive Officer)**

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO  
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, John W. Morrison Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of One Stop Systems, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) [paragraph omitted in accordance with Exchange Act Rule 13a-14(a)];
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 8, 2019

By: /s/ John W. Morrison Jr.

**John W. Morrison Jr.**  
**Chief Financial Officer**  
**(Principal Financial and Accounting Officer)**

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of One Stop Systems, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2019, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steve Cooper, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: August 8, 2019

By: /s/ Steve Cooper

**Steve Cooper**  
**President and Chief Executive Officer**  
**(Principal Executive Officer)**

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of One Stop Systems, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, John W. Morrison Jr., Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: August 8, 2019

By: /s/ John W. Morrison Jr.

**John W. Morrison Jr.**  
**Chief Financial Officer**  
**(Principal Accounting and Financial Officer)**